DCB Bank Limited Q3 FY18 Results Conference Call

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MANAGEMENT: MR. MURALI M NATRAJAN – MD & CEO, DCB BANK
MR. BHARAT SAMPAT – CFO, DCB BANK

Moderator: Ladies and gentlemen, good day and welcome to the DCB Bank Limited Q3 FY'18 Earnings Conference Call. Joining us on the call today are Mr. Murali M. Natrajan – M.D. and CEO, DCB Bank Limited and Mr. Bharat Sampat – CFO, DCB Bank Limited. As a reminder, all participants' 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 and '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Murali M. Natrajan. Thank you and over to you, sir.

Murali M. Natrajan: Good Evening. Thanks for joining this Investor Call today. I have my team here in the Board Room. I hope everyone has received the 'Press Release' and 'Investor Presentation'.

So I am ready to take on questions right away. So let us start with the questions.

Moderator: Sure. Thank you very much. We will now begin with the Question-and-Answer Session. We have the first question from the line of Anup Gupta from Perfect Research. Please go ahead.

Anup Gupta: Sir, the NPAs are consistently inching up for last five quarters. So can you please share your views on it and what actually you are taking to resolve the same?

Murali M. Natrajan: So the action of taking resolving NPAs will be recovery efforts and if you notice that our recovery for this quarter and upgrade for this quarter has been phenomenal if you compare to the previous quarters. Last year same quarter we had a sale to ARC. We do not even have any sale to ARC this quarter. The total NPAs while they are going up, we have always maintained that given our business model we are quite happy as long as the Gross NPA is below 2% and Net NPA is below 1%. That is our business model since we are dealing with the SME, self-employed segment. The other point is we must remember that since November 2016, there have been quite a lot of changes in the country and many of the SMEs have to undergo adjustment to the new way of doing things. That has also put on pressure. You talk about demonetization, GST, RERA, so many things have happened in the country. You also please notice that we hardly have any restructured book and that has been the case for the last many years for us now.

Moderator: Thank you. We will take the next question from the line of Ashish Sharma from Enam Asset Management. Please go ahead.

Ashish Sharma: Sir, just on the growth aspect, we have seen in the previous quarter the growth was subdued in the last quarter from 20% to 28%. Just some color on as to post all the GST and the demon like disruption, how do you see the SME market sort of evolving? Second question would be on this cost-income ratio, given that we have slowed down our incremental branch expansion, I think most of it is already done, but we are still seeing some bit of elevated cost-income ratio, when do you see that sort of inching downwards, just some color on that sir?

Murali M. Natrajan: First of all, please remember that we have one-time cost of Rs.5 crores this quarter on raising of capital, including rating agency cost, etc., So that is unlikely to reoccur, that is #1. #2, when you add branches, you do not get the entire cost in the quarter the branch is put because you are adding people, some people are joining in the same month, some people are joining three months later, so till the branches reach the full bloom capacity, the cost continues to build. When we look at branch-by-branch performance, we have a very detailed metrics on branch-by-branch performance, whether it be un-banked location or semi-urban location, or urban location, whatever, we have a branch-by-branch monitoring that we do and we have a chart which says what should be the target that should be achieved in month-one, month-two, month-three, month-four like that, all the way till 48-months. When we look at all the new branches that we have put barring some branches, some of them are way ahead of that curve, some of them are slightly below and most of them are following the model that we had put together. Our model is all products, all branches which means whatever products are applicable or possible in a particular catchment area, we put all those products into that branches like gold loan, CASA, commercial vehicles, mortgages. So the cost-income ratio that we are seeing is in line with how we have planned it out and we are unlikely to add more than 10-15 branches in the coming two years which is what I have said in my previous call as well. So cost-income ratio should start to come off, not because we are reducing the cost but more because the volume starts to come up in the branches that we have installed. The other thing you have to notice is we are also dealing with certain issues, for example, security guard costs are determined by what government determines as the minimum wages to be paid to security guard. So you have security guards and all of sudden the cost goes up. So these are all surprises. Similarly, GST is 18% whereas we are paying lower on Service Tax. So that has started hitting us from July. So many of these surprises keep coming. So we have to factor in all that. So as far as we are concerned, we do not see any issue with the cost that is building up, we are focusing on getting the volumes up on the branches that we have put. Now you asked the question about our asset growth. Now let me put it this way, I cannot give you any guidance on what would be the asset growth this quarter, next quarter, next year and all. All you have to do is please see our Balance Sheet in 2014 December, compare it with 2017 December. You will see we have more or less doubled. That is exactly our intention going forward also. We are trying to double the balance sheet in 3-3.5-years give or take some three months, don't hold it to the exact number. The thing is that in our plan all of a sudden three months we lost during demonetization, then during GST there is a lot of adjustment that the whole country was going through. So you lose time. So those are interruptions that keep coming. So all in all we are looking for 3-3.5-years to double our loan book and that is where we are working towards.

Ashish Sharma: My question was more on how good is the environment from a growth perspective because we have seen you go down to 20% and now rebounding to close to 28%. So have we seen given the disruption in the economy and in the SME sector, is the market now conducive enough for you to grow at the pace…?

Murali M. Natrajan: We have to make a lot of adjustments. We have to change our credit policies to exclude certain types of customers which we may have been doing say prior to December 2016 or even before 2017 July. So we have to do a lot of changes to our credit policies to make sure that whatever is the environment developments, we are in line with that opportunity that are coming up. So I would say that yes, there seems to be some improvement, but do not forget that there is a lot of capacity also we have added. So some of the growth also is because of the capacity that is building up. If we put a relationship manager this month, he takes about 3-6-months to perform. So relationship managers and sales people that we would have put 6-8-months ago would all be becoming productive as we move along. So that also is reflected in the volume.

Prakhar Agarwal: This is Prakhar from Edelweiss. A couple of questions from my side; first, there have been reports regarding some pressure on LAP segment especially. Your thoughts on the same?

Murali M. Natrajan: Since November 2016, self-employed segment has been under some pressure and please remember that we are dealing with self-employed of small ticket size, we have an approach where we say that not too many loans should be done greater than Rs.3 crores, so our average ticket size ranges somewhere around Rs.40-50 lakhs. Many of these customers had to adjust for these demonetization, GST, etc., that is one issue. Second issue is that there is huge amount of competition. So they tend to over extend themselves because there is finance available, somebody is happy to give a top up, somebody is happy to give unsecured lending and so on. So I would say that to certain segments of LAP, there is definitely delinquency pressure. Wherever we face problems, our NPAs had gone up and we seem to be on top of it, our recoveries are looking okay, I hope we can continue that trend in fourth quarter as well.

Prakhar Agarwal: Just a continuation to that; which particular segment of LAP wherein you are seeing some pressure?

Murali M. Natrajan: Big ticket LAP seems to be under lot more pressure, customers who have more than say Rs.3 or Rs.4 crores outstanding and they have over borrowed or taken more unsecured loans and all, seem to be under some stress. When I look at our LAP portfolio, wherever we have any loan which is greater than Rs.2 or Rs.3 crores and it comes under stress, it becomes a lot more difficult to recover those loans.

Prakhar Agarwal: Second on margins. So we have been seeing some pressure on yields as such. Any ballpark number as to what is our target margin range that is probably anticipated?

Murali M. Natrajan: We will keep working on how to build a business model on 375 basis points. Currently it is about 400-odd basis points. We had some benefit of some of the refinances coming at a slightly lower rate. Going forward, I do not see too much improvement in cost of funds, but there have been no reduction in pressure in terms of competition trying to drive down the yield. So I do think that next two, three quarters, we have to see how the NIMs are but my expectation is that the NIM could be slightly lower.

Prakhar Agarwal: What is the position of your book is linked to MCLR as a whole?

Murali M. Natrajan: Suppose we talk about commercial vehicles, it is fixed rate loan, if we do tractor, it is fixed rate loan. So there are so many buckets that I do not think I can give you that information on this call.

Prakhar Agarwal: In terms of liability, when we look at some of the peer banks traction like SA growth over there have been relatively higher than what we have seen.

Murali M. Natrajan: Please check, guys who are paying more than 4% for all buckets see their traction versus what we do. We pay above 6% only for Re.1 crore and above SA which are usually institutional deposits, very few HNIs coming there. Below Re.1 crore, we pay only 4%. Compare our SA growth post demonetization how it has performed, I think we have grown SA by at least about 12% or 15% which despite the fact that a lot of money which came in demonetization actually have exited. We are pretty happy with our CASA performance. We believe that the base effect of the demonetization would wear off this year and hopefully next year it will be back to normal growth.

Moderator: Thank you. We will take the next question from the line of Aalok Shah from Centrum Broking. Please go ahead.

Aalok Shah: I had a couple of questions and maybe starting with the last one first. On CASA, you talked about base effect kind of wearing off in this year. But as we look into 2019 and '20, the CASA target that we would have in our mind?

Murali M. Natrajan: Ideally, we would like to maintain 25% as the CASA ratio. So let me explain how we do CASA -- We have a target given to every branch depending upon the category of the branch on what is the retail CASA that they have to grow every year, what are the new customers they have to get, what products they have to sell. Usually the sales managers and front line will not be able to make their incentive if they do not achieve their CASA target. The branches which are large which are like in semi-urban, urban areas, tend to do a much better job on CASA than smaller branches because the population itself is pretty less. In those areas, CASA growth depends on some of the smaller government agencies, panchayat and all giving us some support in terms of keeping their float with us. There is a lot of hard work, you start working on it today, you might land up with the success in about six months' time and all, because it takes time to breakthrough those relationships. So we have a strategy for institutional deposits, we have a strategy for individual deposits, we have a strategy for current account. All that is all translated into goals to the various branches and it is monitored on a daily basis on how they are performing. So all that put together we believe that we should be able to keep CASA at 25%. The first year after the disruption that we will be facing in 2018-19. So we will see how the momentum goes, but at the moment we have confidence.

Aalok Shah: I know you do not disclose this number, but would it be safe to say that our average daily CASA ratio would be somewhere closer to this or maybe 100, 200 basis points below this number?

Murali M. Natrajan: Let me put it this way; our relationship managers are measured on averages, not on EOB, that is all. If they do some gaming on the system by bringing CASA end of the month and all, there will be no incentive given to them on that.

Aalok Shah: The second question was on growth. You talked about SME growth where if I look at on YoY basis, there is a strong growth, even on Q-o-Q basis that is like 7% pick up and then when I also kind of look at my retail and within retail mortgage portfolio, that is kind of seen some pick up. Would it be safe to say that incrementally these two pockets and this being our niche areas would kind of outpace overall growth for our overall portfolio?

Murali M. Natrajan: I am not able to tell you that. All I can say is that we are focused on self-employed as a segment. So the pie chart that you see on Page #10 in our 'Investor book' more or less that is how the pie should look even if we double the portfolio.

Aalok Shah: So trying to put it differently; when I look at SME plus Retail today is close to 66% of the overall portfolio and we have done this number even closer to 68-69% in the last…?

Murali M. Natrajan: It will be in that range. Surprisingly, what we are finding even though we have not expanded our corporate team at all, it is the same team that existed give or take one or two people in the last whatever number of years. Because so many banks are in a challenging situation because of PCA and so on, we are getting some really high-quality corporate in our portfolio. So we are quite pleasantly surprised as well as happy about it I would say.

Aalok Shah: Now that you have talked about corporate portfolio. What would be the ticket size and the nature of this exposure?

Murali M. Natrajan: Please do not take it any wrong way, I just believe that no corporate should be given more than Rs.100 crores ever. So therefore, our ticket size usually range between Rs.20 crores to Rs.50 crores, most of them would be either consortium or multi-banking, some would be like LRD proposal kind of thing. So, it depends on what kind of opportunities come. We do not give it to any infrastructure and all, whatever infrastructure loans and all we have had in the past that is what continues, we have not made any major new sourcing of those kinds of loans.

Aalok Shah: So more of working capital kind of loan?

Murali M. Natrajan: More of working capital or term loan which are short-tenor term loans, plus some working capital that kind of arrangement would be there and slowly and steadily we are finding that we are getting very good quality corporate.

Aalok Shah: Yes, because if I look at the movement in large corporate, it has kind of been an upward trajectory and as you rightly mentioned space is kind of got vacant because of some PSUs?

Murali M. Natrajan: Yes.

Aalok Shah: On branch or overall cost side, would it be possible to kind of tell me the employee count? Where I am coming from is…

Murali M. Natrajan: It is about 5,600 employees we have at the moment. So we have added approximately in one year about 800 employees.

Aalok Shah: When I look at my employee per branch count…?

Murali M. Natrajan: We do not work on that basis, our employee per branch would be very high if you compare with the Federal Bank or City Union Bank, our model is very different, I do not know what all the products they do, we do many products, we do commercial vehicles, we do tractors, we do gold loan, we do construction finance, SME, MSME mortgage. So what happens is that when we choose a particular branch, we look at what all the relationship manager or sales people that we have to put in the branch and we put all of them and we have tracking for all of them to see whether they are able to perform or not. So we would be probably 20 per branch or something whereas City Union Bank would be 10 or 12.

Aalok Shah: When we kind of look at recoveries this quarter, I am sure there will be lot of granular part of it, but anything specific to look into it in terms of any space where we have seen considerable amount of recovery?

Murali M. Natrajan: No-no, our loan sizes are average Rs. 40-50 lakhs, recovery is also like that only, very granular recovery. So we do not have any big ticket recovery, except for one restructured loan, which I have already mentioned in my press release which went from restructured standard to NPA, this account has been with us for the last if I recall almost like 10 or 11-years and this has also got affected by the various changes that happened in the country and they were not able to service their interest or installments, so that went into NPA, other than that, it is all granular items.

Aalok Shah: If I could ask the restructured sector there?

Murali M. Natrajan: There is no sector. They are doing some job work for commercial vehicles and other companies. So that is what has gone into some trouble for them.

Aalok Shah: The slippage run rate, barring this quarter we are…?

Murali M. Natrajan: Slippage run rate is in the range of 2-2.1 ignoring the Rs.15 crores or something like that of corporate loan that has slipped, otherwise we are in the same range, some quarter it can go to 2.1, 2.2, some quarter it can be at 1.8, it is very difficult to exactly say that what range it would be, all I am saying is that we are working towards making sure that our Gross NPA is below 2, Net NPA is below 1.

Moderator: Thank you. We will take the next question from the line of Janvi Goradia from Motilal Oswal. Please go ahead.

Janvi Goradia: This quarter we have seen very good traction on fee income. If you could provide some insight into that?

Murali M. Natrajan: Do not draw a trend line based on that immediately but whatever work we are doing on various items like health insurance, like insurance, mutual funds, our focus on making our ATMs more profitable, Trade, FX, all those items have contributed little-by-little, there is a slight base effect I would say is in the core income, because if you look at the third quarter of last year our ATM fees is very low, that is because we have to shut down the ATMs on demonetization. So if you see the ATM fees, will look much higher this quarter. Other than that, we have seen pretty decent work on fees. We hope that we will continue that trend.

Janvi Goradia: There is no one-off?

Murali M. Natrajan: No, on the other hand not just core fee, in total fee I think we have got much better income on our money market last year same quarter versus this year because G-Sec rates have actually moved up this quarter.

Janvi Goradia: Earlier in the call you mentioned that cost of funds you do not expect them to go down further, but we have also revised our FD rates very recently. So should not that provide some sort of cushion?

Murali M. Natrajan: No, I think we have kind of tweaked some buckets in FD, somewhere we have gone up if I am not mistaken. So cost of funds according to me would either stay where here or it is likely to go up as I see it.

Moderator: Thank you. We will take the next question from the line of Rohan Mandora from Equirus Securities. Please go ahead.

Rohan Mandora: Sir, just to take it forward from a previous question, if you could give some broad quantification on the fee income in terms of how it is spread between loan book and third-party transaction fee, liability fee?

Murali M. Natrajan: We have disclosed certain details in page #8 and that is all the details we are able to provide to you, so we have given you Commission, Exchange and Brokerage which includes everything from ATM fee to processing fee to banc assurance and all that comes into that case. This is the detail we are providing to all the investors.

Rohan Mandora: I was just wondering I could get some share like a loan percentage about how that would have moved YoY, Q-o-Q?

Murali M. Natrajan: We are not giving those details. All I am saying is that there is no one-off in this and there is a granular increase in all the lines.

Rohan Mandora: Sir, on the non-employee expense, Rs. 5 crores was one-off expenses that we incurred. Anything else which was one-off in there?

Murali M. Natrajan: No, we would not go into the real granular into everything but the broad number if there is anything that affect us we will always disclose it, whether it is one-off interest income that we have received because of income tax, we disclose those numbers.

Rohan Mandora: What will be the incremental yield say in the mortgage, corporate and SME segment?

Murali M. Natrajan: We have given the yield number in Page #11, 11.25 is our yield on all advances put together.

Rohan Mandora: That was on the outstanding portfolio but currently whatever incremental lending that we are doing…?

Murali M. Natrajan: It depends, I mean, some segments will have higher yield, some segments will have lower yield, there is a risk weighted pricing model that we have. So customers who we see from our model is slightly risky will get charged 25 basis points higher, customers who have very good track record and cash flows and so on might have low. So very difficult for me to say exactly. So that is the composite number that we have presented here.

Moderator: Thank you. We will take the next question from the line of Darpin Shah from HDFC. Please go ahead.

Darpin Shah: In October '15 we had guided on certain parameters on how our ROEs and cost-income look by FY'19, now that we have completed a branch network, and in the interim there are a couple of major events which have happened in the country. Would you like to revise our guidance for FY'19?

Murali M. Natrajan: It is too early to revise it. Yes, we have got disruption of at least three to six months because of the major events that happened in our country. So I would say at the moment the team feels confident of moving towards that goal. So if there is any blip, we will definitely tell you, but the fact is I look at it two different ways – one is as to what are the things that we said in October 2015, the other thing is what are we looking at from 3-3.5-year perspective, how this whole loan book will grow, how the deposits will grow, how the business will pan out. So I would say that looking at how we progress from December '14 to December '17, despite whatever happened in between we feel confident that in 3-3.5-years we should be double or close to double of the loan book without changing the mix of this portfolio.

Darpin Shah: Anything more on cost-income if you can add, you mentioned about 55% band of FY'19?

Murali M. Natrajan: Our first target is to reach that particular goal in the fourth quarter of 2018-19 and then if the Board permits we will be able to give further guidance on that.

Moderator: Thank you. We will take the next question from the line of Rahul Maheshwari from IDBI Mutual Fund. Please go ahead.

Rahul Maheshwari: No doubt the CV and construction finance, the growth rate was good enough though it contributes less as compared to the other segments, but can we expect the same run rate if at all, all the macros and all this stays of these two segments?

Murali M. Natrajan: Commercial vehicles is amortizing loan, it is almost like treadmill sometimes because it is a three, four-year kind of loan. So what happens is that if you originate 100 units, 30-40 units run off in that particular month. So we have to keep on adding more capacity and get more volume for us to have similar kind of growth. Having said that, commercial vehicles, all the robustness that we are seeing recently we are confident of maintaining it at about 4-5% of our total portfolio and we are doing it in a very steady manner, focusing on good segments which gives us the priority sector lending advantage and all. Construction Finance, our ticket size is very small…Rs. 3, 5, 10, 15, crores, like that, we are very careful about not extending ourselves beyond that kind of loan size. What is happening is those who are quickly converting themselves into discipline of RERA, we are finding that the loan repayments of those customers are faster. So the book even though we originate lot of loans, lot of them are actually prepaying because they are constructing faster, they are able to sell faster especially in a segment where it is like Rs. 40-50 lakhs kind of flat cost.

Rahul Maheshwari: They are lending to the reputed builders and construction.

Murali M. Natrajan: Construction finance, we do to builders who have a track record, there is a parameter that we have, we use their parameters to check their track record, we do certain external agency verification of the builder, we do site visit, we do a lot of due diligence before we actually extend the loan. What I am trying to say is that some of these builders who are very good, they have converted themselves to the RERA discipline quite well and they are also seeing good sale. Then what happens, whatever money that we have said that they will draw down...first of all they do not draw down the full amount and then they repay also the loan faster. So I do not see this book growing too fast given that we will be very careful in terms of who we give this lending to. Having said that, it will still be about 3-4% of our book.

Rahul Maheshwari: Can you give what kind of credit rating or profile of corporate segment in terms of 'AA' or 'BBB', any breakdown of corporate?

Murali M. Natrajan: We do not provide that data. We are very careful in corporate banking and we have been maintaining this at about 15, 17% of our total book. Even if we double our book, I still think it will be less than 20% of our total book. The top-20 advances in our Bank is less than 7%.

Rahul Maheshwari: On the mortgage side, as you earlier also did a commentary, you are going cautiously right now and going forward also you are finding pains this run rate of 20, 22% would be maintained kind of thing?

Murali M. Natrajan: 20, 22% run rate should be possible in mortgage. After demonetization and after GST credit policies have been tweaked and our monthly origination has been readjusted. A lot of segments which was quite okay before this, at least to us, does not seem to be okay, but there may be other financiers who may find it acceptable, I do not know.

Rahul Maheshwari: Within two years, excellent in terms of the branch expansion you have done. So can you give a breakup in terms of the new branches which have been added in this one and two years, what kind of breakeven or productivity or ROA or ROE has been achieved at least for a one year back branches so that we can get…?

Murali M. Natrajan: At a branch level we do not calculate ROE, ROA. At a branch level we only monitor breakeven, year-to-date profit, and cost-income ratio.

Rahul Maheshwari: So for new branches what kind of branch profitability has come?

Murali M. Natrajan: Like I mentioned early in my call, what we do is we say that every branch will do what volume on month-on-month basis all the way to 48-odd months because sometimes after about 24-months if the branch is on track, you do not need to really worry about the profitability of the branch… although we do that because it has crossed all the hurdles. So barring a few branches, all the branches that we have put in whether it be unbanked area or rural area, it has followed the model. So other than that we do not disclose any data on a branch wise basis. If it had not happened, our cost-income ratio would have gone for 70% or something like that. You can see how much cost we have incurred on these; cost at least Rs. 60-65 lakhs on an average per branch and you look at the volume also, we have been growing our volume. If you look at our branches in December 2014, if you see Page #1, it is 130 branches we had in say March 2014 and it is now 311 branches, look at the Balance Sheet, it is from 12,000 it has gone to 27,000.

Rahul Maheshwari: So the intention was that going forward as you said that per annum the branch expansion would be taking place in 10-15 kind of thing and the cost–income ratio would not be declining. So what kind of additional expenses would be incurred in terms of the efficiency kind of thing if at all the branches are not expanding?

Murali M. Natrajan: Like employee annual salary increase would be there, inflation related cost would be there, so of the branches would have completed three years, the rental cost would go up by 5, 7, 10% depending upon what we have agreed with those. So all those costs would naturally come in for our bank. On other hand, maybe the branches which are completing three years and all some depreciation also will fall off. So those will be the moving parts for the cost.

Rahul Maheshwari: But this is the peak cost-income ratio… 62.3?

Murali M. Natrajan: We hope so and we believe that we are either peak or near peak on the cost-income ratio.

Rahul Maheshwari: Any target for FY'19-20 for cost-income?

Murali M. Natrajan: We have already published; if you see our October '15 guidelines, fourth quarter of 2019 we want to exit at 55% or below.

Rahul Maheshwari: What is the non-fund based exposure in your book and what kind of nature of that exposure is there?

Murali M. Natrajan: Bank guarantees, LCs, little bit of FX derivatives, mostly related with SME segment and a little bit to the corporate segment.

Rahul Maheshwari: Any stressed account of non-funded which has been into your asset quality?

Murali M. Natrajan: At any point in time in the last nine years that I am going to complete in the Bank, we have had some two, three corporate accounts in some stress and we have been managing that, some we have exited, some have repaid, things gone and once in a while we have this mishap like what has gone into NPA which we are also confident of recovery. I have lot more confidence of recovery in NPA in SME than I have in corporate because in corporate mostly other banks also will be part of the lending and to get to some concerns on how to proceed forward, takes a lot of time. That is why the recoveries are somewhat slow in corporate.

Rahul Maheshwari: That is appreciated that the recovery you can do for SME. So going forward can we expect the recovery rate would be higher than the slippage rate for you?

Murali M. Natrajan: At some point it will be. I do not know at what point it will come like that. If you see our SME-SME slippages, it has been very minimal, the slippages have come mostly in mortgages in the last year and a half, that too a lot of the portfolio got affected in the smaller segment because of demonetization and GST.

Rahul Maheshwari: But your slippages have increased in Agri and Inclusive Banking. Any…?

Murali M. Natrajan: That is because you have to lend for microfinance institutions, about 5% of our lending is to microfinance institutions to complete our weaker section priority sector which got into a lot of challenge because of the loan waiver, demonetization and all. So I think …

Rahul Maheshwari: Now it has been stabilized according to you?

Murali M. Natrajan: It should stabilize, I think things are improving, but whenever it is unsecured, recovery will be somewhat slow.

Moderator: Thank you. We will take the next question from the line of MB Mahesh from Kotak Securities. Please go ahead.

MB Mahesh: Just two questions; one, when you are going in for recovery today in your LAP portfolio, could you just give some color as to what kind of recovery rates that you are seeing out there or is it mostly through settlement that you are engaging with the borrower? Second is on the SME side, there has been some pickup in credit. Have you seen most of this is coming on the back of GST related shortfalls which the customers are seeing or is there some pickup in economic activity in the company that you are working with?

Murali M. Natrajan: I will answer the last question first; part of our SME growth is because of the capacities that have come in branches and all and then since we are doing a lot of neighborhood banking there is a lot of SME business that we are able to attract. 20% to 25% of our SME business is all either wholesale trade or retail trade, the rest would be on manufacturing, some services and so on and so forth. In the past we used to ask for VAT receipt for determining the customers' sales performance, needs, etc., now we are trying got get the GST details for establishing the same thing. Whether there has been any economic pickup and all, very difficult to say according to me, we will see one or two more quarters, but I would say that in SME working capital lending that has gone more than Rs. 2,000 crores or something now, we feel more positive about it.

MB Mahesh: Is there more credit utilization levels or is it more newer penetration that you are seeing of customers?

Murali M. Natrajan: I am seeing both, in existing portfolio we are seeing more credit utilization as more business is being throughput is the banking account which they may have been doing in cash. At least the 15,000-odd customers have been met in the last six months, many of them seem to believe that it is better to actually do a throughput through the bank rather than do it in cash. So whether it is all actually translating into full-fledged change, I am not sure yet. So SME I feel positive and especially those who are making the change to comply with GST and do all the necessary things, I think there is some improvement we can definitely say it is happening.

MB Mahesh: Now just one clarification; when you are speaking to your borrowers, you are saying that this year revenues that they are likely to report is going to be meaningfully better than last year.

Murali M. Natrajan: Sales definitely they will report, I am sure they will find ways of managing their profitability…again, we decided that even before demonetization and GST I can tell you that it is very difficult to address the needs of a customer who has too much of cash, it cannot be trusted, so it is very difficult for me to lend to those customers even before we used to lend to customers only with VAT receipt and proper records and things like that. He may not have proper income tax record but definitely on sales side he has to have very good record. Coming to LAP, first of all, let me put it this way; we as a team and management believe that unless the customer is a fraud or he is absconding or he has completely collapsed in terms of his business, the only best way to do your recovery is to cooperate with the customer, work with the customer and realize your asset value rather than try and do some long-drawn legal process. Of course, we will file SARFAESI, of course we will send him legal notice, that is more to keep that option open and keep the pressure on that customer. Now when I say this, I even mean bigger customer which are corporate customers. I would like to believe that seeking the cooperation of the customer gets better asset value than trying to fight with him on the asset. That is our go-to approach. So if you look at our LAP recoveries and all, we would actually work with the customer, we would have sent him the notice and all, we would tell him why do you not settle it because if he sells property we will realize less value and then he would not even get the surplus that might be there or find him some buyers who are good and tell him that why do you not use this buyer to take it. So there is multiple ways in which we deal with the thing. Very rarely we actually auction the property.

MB Mahesh: The reason why I am asking is that if assets are now being kind of put into the market, just trying to see if you are able to kind of recover the value which was initially estimated on that property?

Murali M. Natrajan: If the value is 100, the moment the bank is involved and trying to sell it and all, automatically it will become 70 because they know that the bank is trying to sell. So it is better to cooperate with the borrower and find the buyer, he will also get some balance of what he has repaid us, he will also get some surplus, otherwise it is a lose-lose for both borrower and bank.

Moderator: Thank you. We will take the next question from the line of Dhaval Gada from Sundaram Asset Management. Please go ahead.

Dhaval Gada: Just a couple of questions; firstly, just wanted to understand the experience on the Personal Loan segment and in the pie chart we do not see it is mentioned, I believe it would be less than 1%. Any thoughts of how it is scaling up in the portfolio quality?

Murali M. Natrajan: We have less than Rs.100 crores if I am not mistaken on Personal Loan, probably Rs.50 crores, I do not know, something like that. It is a very small team. We are mostly trying to do cross-sell to our own existing customers who may otherwise be taking Personal Loan from other bank. The ticket sizes are very small, it is not business installment loan of Rs. 35 lakhs and that type of thing, it is only Personal Loan of Rs. 3-5 lakhs on an average and the experience so far has been very good but it is too early to say, we are very cautious about how we are going to scale up this business. In any case, even 3, 5-years from now it is unlikely to be more than 3-5% of our total portfolio.

Dhaval Gada: Second question just a little broad-based. So currently after the branch expansion, in your assessment what would be the capacity utilization, in the sense that this capacity adjusted for cost inflation and basic addition, what kind of loan book we can achieve?

Murali M. Natrajan: It is a very fairly complicated and intelligent question, but I will try to give you the way I see this issue; you look at what is the average business of City Union Bank per employee. I think it is about Rs. 13 crores, if I look at ours it is probably less than Rs. 8 crores. So the way I see it is that is the utilization we want the rate in the next two to three years and remember we are trying to build this on small ticket business…when I say small ticket not like micro finance, I am talking about like average ticket size of Rs. 30, 40 lakhs, that type of ticket size we are trying to build. City Union Bank is an example I have taken because we believe that it is a good model although they do not do all the products that we do, but we are quite impressed with their productivity, cost-income ratio and so on. So I would say there is a lot of capacity that we need to kind of utilize. Having said that, there are branches that are doing astonishingly well even though they are new. So we will end up giving more headcount to them in the coming months, years, that is #1. #2, some of the portfolios that we do are amortizing portfolio, for example, commercial vehicles, for example, tractors, for example, mortgages. Now if we have to maintain the growth in that we have to keep adding some capacity to those so that our new sales is good enough to grow the balance sheet at that level. So there are multiple things happening but our go-to is at least try and reach the City Union current productivity level in two to three years.

Let us take the last question because I have another conference call coming up.

Moderator: Sure. Due to time constraints, we will be able to take one last question. The last question is from the line of Ramesh Rachuri from Scient Capital. Please go ahead.

Ramesh Rachuri: One thought that I had was if we see an interest rate regime today morning Axis Bank increased its MCLR rate by 5 basis points, maybe that is the start. The basic point is the strategy on which you have run by maintaining CASA of around (+25%) except in March 2015 when it is below that, so is that a feasible strategy going forward particularly if interest rates rise and concomitantly in that regime how do you see credit cost panning out?

Murali M. Natrajan: Credit cost we will approach separately. Credit cost barring any major surprises that may happen once in a while anyway smaller corporate book. We will see that we will be pretty much in control of the rest of the retail and SME portfolios because the way we manage the portfolio. As we see any issue in any pocket coming up, we take actions both corrective actions and recovery actions on those portfolios. So therefore, we see that pretty much as predictable in terms of how it will come. So credit cost maybe maintain at about 50, 60 basis points and that is where we are aiming to keep that credit cost. When interest rates go up, there is always pressure on credit cost but such a cycle we have already gone through about three, four years ago and we did not see any major issues on it. When we are dealing with say mortgages, there customer has got self-occupied property. I do not believe that they default because of their interest rate, some would, but not in any meaningful manner. Now with respect to CASA ratio, our intention is to keep the CASA ratio at about 25%. There is a lot of work going on, on products, distribution, sales monitoring, sales tools, training and so on across the footprint. Some of them are yielding good results, some of them are still work in progress. So like I said right in the beginning of my call, if RMs do not achieve their CASA, they will struggle to get their incentive. So we believe that that would help us to keep our cost of funds in check. But yes, the cost of funds are going up and it will go up shortly and then we will have some challenges coming up in fixed rate portfolio, so we have to manage all that as we move forward.

Okay. If there are any questions that I have not been able to answer, sorry, because I have a staff conference call starting in about five minutes for which we have to prepare, so we are not able to take any further questions, but please feel free to write to Gaurav or Bharat and we will be happy to address it on one-on-one basis. Thanks very much for attending this call.

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