DCB BANK

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Moderator Ladies and gentlemen good day and welcome to the DCB Bank Results Conference Call. As a reminder for the duration of this conference, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call, please signal an operator by pressing "*" and then "0" on your touchtone telephone. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Mr. Murali Natrajan – MD and CEO, DCB Bank. Thank you and over to you sir.

Murali Natrajan Thank you. Good afternoon everyone. My name is Murali. I am joined by Bharat, who is the CFO of the Bank, Rajesh Verma, the Head of Treasury, Sridhar Seshadri, who is the Financial Controller and Meghana, our Investor Relationship Head.

So let me spend about 10 minutes to explain our 1st Quarter results and then I will open up the floor for questions.

The Quarter 1 profit was Rs. 8.83 crore, this compared with last year loss of Rs. 2.91 crore. As you remember, we entered into the profit territory in the 2nd Quarter of the last financial year. The previous running quarter which is the 4th Quarter of the previous year was Rs. 11.35 crore, so there has been slight dip in the profit in the 1st Quarter.

One of the highlights of the quarter is in this quarter; we have absorbed Rs. 3.25 crore additional provisions due to change in RBI provision norms. So if you recall in the credit policy, they had announced new provision norms. So for the entire stock of NPA, we had to apply the new provision norms and therefore we had to take an additional provision of Rs. 3.25 crore, which I think is basically a one-time for this particular quarter. I would say in some ways this has not been an easy quarter because there was an increase in the savings account interest rate by 50 basis points and generally, the interest rate and cost of deposit was on a steady uptrend. So that is where we had to kind of moderate our growth because the opportunities for growing advances were limited with the kind of interest rate that was prevalent. We also did an annual staff cost increase and we have started increasing the headcount for gathering more CASA deposits. We have been steadily building higher headcounts in the branch banking for gathering CASA deposits, so that has also reflected in our staff cost. We were able to maintain NIMs, primarily on account of timely re-pricing and some bit of product mix but generally it was a very big challenge to be able to maintain the NIMs and we are still seeing pressure on cost of deposits and we will wait and watch as to what happens in the monetary policy later this month.

Underlying provisions continue to decline and the provision line would have been much better than Rs. 7.69 crore, had we not had to take the Rs. 3.25 crore additional provisions because of the RBI norms change and also because we had two corporate accounts which became NPA in this quarter. We are confident of resolving one account in the current quarter. The other loan, we have taken provisions in this quarter. However, the underlying book in terms of MSME, SME, retail, all are absolutely in good shape as of now. And although we have increased interest rate on loans, we have not seen any stress on these portfolios and we continue to monitor the account to see if there would be any stress for further increase in the interest rates.

Recovery and upgrade especially in the retail area and Personal Loan continues to be good and on track. Like I mentioned Cost of Fund increase is a bit tough and it doesn't look to me that there will be any easing up of this in the next 3-6 months or so. Cost increases were primarily on account of headcount to step up CASA growth, the reason we did that was, we are now seeing some reduction in provisions, which was not what we had last year. So we have taken the liberty of investing that in cost in order to step up our low cost Deposit, which is CASA. And we are confident that we would be able to do a much better job in CASA.

The CASA ratio dropped to 33%, is still very much within our strategy of always keeping CASA above 30%. The reason why it has gone to 33% is we have raised a lot of Term Deposits from the customers in order to somewhat reduce our reliance on wholesale borrowings as well as to repay a part of the sub-debt.

In terms of Other Income, last year in the 1st Quarter, we had a one-time gain of about Rs. 5 crore for transferring the securities from HTM to AFS. That opportunity was not there this year. Additionally, the RBI rules were such that, we were not able to invest in mutual funds beyond 10% of our net worth. Therefore, we also had to reduce that business that had an impact on the Other Income. But the underlying Other Income in terms of Bank Assurance, Trade, processing fee, etc., are granular and continuing to be solid and as we increase our customer base, we are confident of making progress in the coming quarters.

We also shifted our Corporate Office from the existing to a new office and that resulted in a write-off of Rs. 1.4 crore of the premises that we could not recycle, so that also was hit this particular quarter, so that is also a one-time kind of a hit.

All in all, somewhat a difficult quarter from an interest rate perspective and we made up some of the NIM by doing the re-pricing. We are continuing to focus on SME, MSME and Retail Mortgages. The Advances growth in year-on-year is 22%, however if you look at last quarter to this year, it is almost flat primarily because in the 1st Quarter, we have Agri Loans getting repaid and also we exited two or three corporate accounts on our own. So the loans that we booked in MSME and SME and Retail Mortgages were not adequate to make up for those exits, so their Balance Sheet was flat from that point of view. However, we are seeing robust tracking in the Retail, MSME, and SME, so we are confident of at least achieving 18%-20% growth this year on Advances.

In terms of reliance on retail funding, we have simple strategy, we are supposed to be higher than 70%. Again, this quarter, we were at about 82%, so we are focusing on getting granular Deposits to fund our Balance Sheet. We also got approval from Reserve Bank of India for 10 new branch licenses, 6 in metros and 4 in Semi-Urban/Rural. We are in the process of identifying premises and putting a plan together for installation of these branches. We have put a cross functional team together to implement these branches in the next six months and that would help us in CASA growth in the coming year. If we do a good on these branches, we are confident that we can go back to Reserve Bank of India and ask for more branches.

Capital adequacy continued to be strong. Tier-I was 11.07% and total Capital Adequacy was at 12.92% under Basel-II. We have approval from the shareholders for Rs. 300 crore of QIP and Rs. 200 crore of Rights. We are in discussion with investors and at an appropriate time, we plan to raise anywhere between Rs. 150-200 crore of Capital in this financial year.

That is what I wanted to share with you. If you have any questions, please feel free to ask and myself and my team are here to answer those questions.

Moderator Thank you. The first question is from the line Sneha Kothari from Subhkam Capital. Please go ahead

Sneha Kothari I just want to know, we have not done any tax provisions in the quarter?

Murali Natrajan We don't need to make a tax provision because we have accumulated losses.

Sneha Kothari Okay and what would be the quantum of this, accumulated losses?

Murali Natrajan We have accumulated losses of about Rs. 380-400 crore, so until we cross that level we don't have to pay taxes. There is a Minimum Alternate Tax that is applicable to us, but, however, if take write-off of our provisions then we don't need to pay MAT as well.

Sneha Kothari Sir, in 4th quarter, you have managed ROA of 0.63% and again in 1st quarter we are seeing a ROA of 0.48%, so where we expect our ROA in the coming quarters and from which area we are planning to improve on that?

Murali Natrajan First of all, in this particular quarter, as I mentioned to you we had to make an additional provision of about Rs. 3.25 crore because of Reserve of Bank of India change in norms. Second, we also had to take a hit of about Rs. 1.4 crore on shifting of corporate premises. Then we also had to absorb the increase in staff cost which we do in April, but staff cost increase happens in just one month, whereas the Balance Sheet growth happens over a period of time. So we are confident of achieving about 70 basis points of ROA this year as well.

Sneha Kothari And sir, how do you see your cost-to-income side in the coming quarters?

Murali Natrajan We are consciously increasing cost, all in the front line Deposit growth especially in the branches. The reason why we are doing it is that, we want to have 30%-34% type of CASA ratio to fund our Balance Sheet. We were not able to do this because we had the burden of provisions till last year. As we see provisions coming off, we are getting the confidence to invest a little bit more in staff cost. These are scalable costs which means that if for some reason, our strategy was not to be successful, I can always scale this cost back, because we are not investing in premises or any fixed cost, it is basically sales people that we are investing in, so we will be able to scale back this cost. So I expect cost-to-income ratio to come down as our Balance Sheet builds up this year.

Sneha Kothari Can I get the duration of the investment book?

Bharat Sampat Duration of investment book, the HTM is 4.62, AFS + HFT is 0.64, modified duration.

Sneha Kothari And risk-weighted assets?

Bharat Sampat Risk weighted assets, Rs. 5,012 crore.

Moderator Thank you. The next question is from the line of Abhishek Kothari from Way2Wealth Securities. Please go ahead.

Abhishek Kothari You are planning to increase Retail portfolio, in your overall Advance portfolio, could I just ask what sort of other income or fee income are you planning to generate out of that?

Murali Natrajan Yeah, our main strategy on Advances is to rely on Retail Mortgages. Retail Mortgages has two components, one is Loan against Property, which is given for business purposes and other is Home Loans. Our principal target market is self-employed, so almost 60%-70% of our loans, in Retail Mortgages are targeted towards self employed. The next item is on SME and MSME, so we have two sales teams, one for MSME and one for SME. Here we give Term Loans for business, working capital loans. Again, it is all on secured kind of loans we give. The kind of income that we are generating is from actually Bank Assurance, we sell Bank Assurance product to our CASA customers and Loan customers. Then we sell General Insurance like health, accident, etc. Then we do Trade, we have trained approximately 30-40 branches for pitching Trade products to our SME and MSME customers. So we also generate Trade income. The challenge for us on growing our Other Income has been that, as we kept stepping up the income, we were kind of hit by, for example, a change happened last year on insurance, Bank Assurance, so the rates of commission have come down. So while we are doing more volume, we still are at the same income level as an example in Bank Assurance. So the strategy is in place and the training and the facilities are all in place. So, we have now even put all these in our scorecards for our relationship managers. So we are confident that we will see traction on this income.

Abhishek Kothari Could you give me your outlook on your Mortgage business, which on a quarter-on-quarter I guess has increased by 19%.

Murali Natrajan Retail Mortgages increased from Rs. 1,081 crore as on March 31, 2011 to Rs. 1,252 crore as on June 30, 2011 growth of about 16%, so we have a pretty good team in Mortgages who are able to and we are operating across about 7-8 top cities in India. We are consistently generating Mortgage with a balance between Loan against Property and Home Loans.

Abhishek Kothari What would be the percentage?

Murali Natrajan In some months, it will 60% in Home Loan and 40% in Loan against Property and in some months it could be even 50-50.

Abhishek Kothari **C**an I have provision breakup and NPA movement during this quarter?

Bharat Sampat **G**ross NPA details are given in page 19 of the investor presentation which we have shared with you and also on our website. Personal loans have come down from Rs. 129 crore as on March 31, 2011 to Rs. 127 crore as June 30, 2011.

Abhishek Kothari **Also o**verall NPA movement, opening, addition, and recovery.

Bharat Sampat Opening was Rs. 264 crore and fresh slippages was Rs. 35 crore.

Murali Natrajan And Rs. 35 crore is primarily two accounts in corporate, no significant slippage at all in any of the other segment.

Abhishek Kothari Both these accounts would account for?

Murali Natrajan About Rs. 28 crore. The rest is normal slippages that happen. And we had recoveries to the tune of Rs. 12.43 crore.

Bharat Sampat And upgrade Rs. 6.3 crore.

Abhishek Kothari Okay. And provision breakup? I mean for NPA and for others that kind of a break if you have?

Murali Natrajan We have only for NPA, there is no other provision.

Abhishek Kothari How much was it?

Bharat Sampat That is Rs. 7.7 crore.

Murali Natrajan And out of that, large part of it would be only for the new fresh slippage of the Corporates.

Abhishek Kothari The Rs. 7.7 crore includes Rs. 3.25 crore?

Murali Natrajan Yeah, which means we had to take Rs. 3.25 crore on the existing stock as per the new provision policy.

Moderator Thank you. The next question is from the line of Elizabeth John from CRISIL. Please go ahead

Elizabeth John Basically regarding the cost-to-income ratio briefly touched up on that, it was largely due to the staff cost. Is it because of this addition in the headcount or also it is because of the salary hike?

Murali Natrajan Since December of last year, we put a plan saying that we need to increase the number of headcounts in the frontline deposits because we wanted to further increase the CASA per branch. You see that there is one of the pages in the investor presentation, which shows CASA has grown from Rs. 17 crore per branch to Rs. 23 odd crore per branch. Our aim is to take it to Rs. 35 crore per branch in the next 2-3 years and for that, what we decided was that now that our provisions are declining, we will put a scalable model whereby, we will add more headcount in frontline Deposit especially for CASA. So the cost increase in staff cost is because of (a) the increase in headcount approximately about 300 odd, we have done in the last 4-5 months. And (b) also because of the annual salary hikes that we do. You will notice that the operating expenses is constant, is quite the fact that we have been building a Balance Sheet that is primarily because we are bringing in a lot of efficiency in the other operating expenses through better utilization of premises, process improvement, and all other kinds of cost efficiencies that we are bringing in. That's the reason you find that to be constant whereas the only item that must be growing is the salary cost.

Elizabeth John And are we even planning to scale up further the headcount in the branches in the frontline Deposit taking?

Murali Natrajan The current branches would stay at what headcount that we have now, but we have approval for 10 branches, so approximately if you take even 6 per branch, I would add about 60-70 headcount more in the coming year.

Elizabeth John And second thing about the capital adequacy ratio, which is currently around 12.92%. I just wanted to understand one thing, I mean if supposedly a QIP does not happen immediately then are we comfortable in that kind of capital to fund our loan book?

Murali Natrajan For this year, if we fund our Loan book through the existing Capital and if we say for example grow by 18%-20%, we probably end up at about 9.5% as Tier-1. And if we want to grow it further, we obviously have to increase capital, but more importantly, we want to implement these 10 branches and once we finish implementing these 10 branches and we are able to convince RBI that we are on a good track, we want to go ahead and ask for some more branches from RBI as per our Retail and SME strategy. So in which case, we definitely need to raise capital for implementing these branches. So we are pretty much planning to raise capital this fiscal year.

Moderator Thank you. The next question is from the line of Prashant Shah from Vantage Securities. Please go ahead.

Prashant Shah I just wanted to ask you, you all are basically focusing on the retail and SME and MSME book, why did you remain sequential, because with your focus it should grow at least to some extent?

Murali Natrajan One of the big challenges that we had in 1st quarter is that, when we analyzed the MSME and SME portfolio, large number of customers have reduced their limit utilization. We have not had exits. So while we cannot call all those customers because there are like small and big customers, we took a sample of approximately 40-50 customers both in MSME and SME and made contact as to why there has been a reduction. There have been various answers, one is for example, that they want to wait for utilization of limits and see how their demand for their product picks up before utilizing further. There have been other instances where they found that since banks are increasing interest rates, it is better for them to put some of their own money and reduce the utilization, so that they can reduce their interest burden. So while we did a pretty good job on new loan origination, the existing book utilization kind of reduced a little bit more than what normally happens in the 1st quarter, at least what we have seen in the previous year. So that's my explanation.

Prashant Shah You mentioned that your Cost of Deposits grew significantly, it was 6.67% against 5.6% in the last year. So did you hike your Deposit rates?

Murali Natrajan We have to. These days if you don't hike your Deposit rates, then there is no chance of you getting a Deposit, so even better rated Banks have slightly higher Deposit rates than us at times in some bucket, so we have no other choice. But again, I don't think we can keep on passing on the increase to customers because we don't want to put a lot more stress on the customer accounts. So we are very cautious when we talk about NIMs at this stage.

Prashant Shah But you don't see your Yield on Advances increasing too much beyond 12% because it's something at 11.9% right now.

Murali Natrajan It is at 11.86%. Yeah it is tough and even now, if we have to increase rate based on any change that happens later this month from RBI, we think that we will be selective in terms of passing on the increases to the customers.

Prashant Shah Your Deposit rates as you mentioned are raised, so have you re-priced all or you still expect some re-pricing still to take place?

Murali Natrajan I think, since September 2010 or something like that a lot of Deposit has got re-priced but say for example, some got re-priced from 7% - 8-8.5%, now those are also looking like that they will get re-priced at 9.5% type of a thing. So for six months, I do expect Deposit rate to continue to be definitely firm, I do not know whether increase in turn but definitely firm.

Prashant Shah Sir, your investment book increased mainly because you invest a lot in a SLR book. Your SLR ratio increased to 34%.

Rajesh Verma We maintain excess SLR and found more opportunities in T-Bill so recently we increased our investment in T-Bills.

Prashant Shah Okay, so it's nothing to do with RIDF bonds ?

Rajesh Verma No.

Prashant Shah It is just basically incremental investment because of the rates being attractive.

Murali Natrajan Yeah, as far as the priority sector lending is concerned, last year we met our priority sector target. Of course, subject to RBI inspection, previous year also we have met priority sector lending target. So I do not expect any RIDF but we will wait for the final report.

Moderator Thank you. Our next question is from the line of Mani Arora from ICICI Securities. Please go ahead.

Mani Arora First of all wanted to ask about the NPA figures, actually it is a 22% sequential jump. Did you have any write off this quarter?

Bharat Sampat Net NPA, we continue to write off from time to time.

Murali Natrajan So, like for example if you have a personal loan of say Rs. 5 lakh and for some reason let's say we settle with the customer at Rs. 3.5 or so because he is in very deep vintage and he is not being able to pay for a long time. In that case the Rs. 2 lakh would be a write off. So like that we have a write off. Apart from that I think, 1 or 2 Corporate accounts of Rs. 3 - 4 crore and all which are like deep vintage, we take a technical write off.

Mani Arora You have an amount which you can probably provide?

Murali Natrajan I can tell you that altogether it's about Rs. 17 crore.

Mani Arora So that probably led to a marginal dip in your Provisional Coverage Ratio and slight increase in the NPA.

Murali Natrajan Yeah. Essentially the increase in NPA this quarter is because of the 2 Corporate accounts that we had. SME, MSME and Retail book is in good shape.

Mani Arora Sir, about the lumpiness of these accounts. Do we have some other accounts, as in which are not critical as of now because probably because of their size, the amount could probably create a problem in future?

Murali Natrajan Yeah, that I always said in all my calls, in all individual interactions with the investors that our main focus is on small SME, MSME and Retail account given our small Balance Sheet.

Mani Arora But Corporate again is 12% or more, right?

Murali Natrajan No, but we have historically dealt with a lot of Corporate accounts, which you noticed in the last 3-4 years, we have reduced our Corporate, especially but we are not growing the Corporate book. And from time to time, there are these challenges that crop up but we are confident of dealing with those.

Mani Arora No, it is just that we are expecting better in terms of bottom line?

Murali Natrajan I have not seen any of this things but in a Corporate account despite best care, at times do become either CDR or some challenge like that.

Mani Arora Sir, another question is on your Agri-portfolio. I just wanted some more clarity because as far as I remember from Q2 FY 11 to Q3 FY 11 we saw a jump in the Agri-portfolio and you talked to me and told that it was because of the seasonality. And if I compare to y-o-y, in Q2 FY 10, I see a similar jump from Q2 FY 10 to Q3 FY 10, but when I compare my last year's Q4 FY 10 to Q1 FY 11 and this time Q4 FY 11to Q1 FY 12, I see a sharper dip. Could you please explain the seasonality factor once again?

Murali Natrajan Sometimes it depends on the compositions. Last year for example, we would have relied more on Micro-Finance, which has much slower re-payments. This year, we relied more on Agri-commodities which have a sharper re-payment, if the customer finds the interest rate has moved up and he wants to liquidate, they have liquidated that. But normally we find that the peak happens somewhere between November to March or November to April and then you should see that again happening from October onwards.

Mani Arora Yeah, again Q3 FY12 could expect Agri thing to rise higher?

Murali Natrajan Because, what happened last year, we absolutely kept away from Micro-Finance, which is more granular and it does not have lumpy re-payments, because whatever happened in Andhra Pradesh. We relied on other products, which has got much more lumpier re-payments.

Mani Arora Do you have any of these Micro-Finance accounts which was previously there as NPA?

Murali Natrajan We had 2 NPAs which we have provided for in our thing. I think we did that in last quarter itself, one was Share, another is Trident. In each, I think we lost about a crore of rupees.

Bharat Sampat Share, we provided it in March, Trident is in restructure.

Murali Natrajan Yeah, so those are the 2 accounts that we had problem in Andhra Pradesh.

Mani Arora Have you paired down your growth guidance?

Murali Natrajan I thought, I always said it is 18% to 20% growth, did I say something bigger than that before. We want to do a lot bigger job on the Deposit side but on the Loan side given the interest rates environment, I do not see the opportunity for us to do and we definitely do not want to be too aggressive at this kind of interest rates.

Mani Arora So, I just want to get some more clarity. First of all you are saying that 18% to 20% growth is understandable. The Deposit mobilization at this point in time looks pretty good, but you will also go in for raising Capital to be utilized for future expansion plans. So net-net, what time you see your growth pickup, probably next year, FY 13 onwards?

Murali Natrajan No, I would say that the Capital raising plans are more directed towards getting our branches up and running and employing more people, like I said another 60-70 people to be put in the branches. Once we do that, we want to be in a position to approach Reserve Bank of India again and ask for more branches so for which we definitely need capital for that. So, to grow 18% to 20%, I think, we have adequate Capital.

Moderator Thank you. The next question is from the line of Amit Ganatra from Religare Asset Management. Please go ahead.

Amit Ganatra One question was on the ROA guidance that you mentioned. So basically you still maintain the 0.7% kind of ROAs for a full year but currently you are at the 0.48% with zero tax. Last year your tax rate was around 27% or so, assuming the similar tax rate prevails then basically 11 bps more so. I mean how do you achieve this 70 bps kind of ROAs because the NIMs also have not fallen for this quarter significantly, whereas your earlier guidance for NIM was a higher falls, however, NIMs have held up so this ROA already incorporates a good healthy NIM. The only area was the operating expense ratio but there your growth guidance is not extremely strong. So what was the ROA?

Murali Natrajan Are you saying that my ROA is likely to be lower than what I said? Is that what your point is?

Amit Ganatra No, what I want to understand is from the current level of for this quarter whatever the ROA that has been reported, which are the areas from where it can improve significantly?

Murali Natrajan Yeah, definitely it will improve because of the CASA growth because that is where I am investing in people. Secondly, it will improve because of the Balance Sheet growth, especially in SME, MSME and Retail Mortgages. Third is, we don't expect a continued increase in cost, we should be able to hold onto our existing cost levels and also I am expecting provisions to be stable at this level or even improve.

Amit Ganatra Key thing is that, if you say that it should improve because of CASA and SME book growth is, that means that the NIMs have to improve from current levels?

Murali Natrajan How to predict a higher NIM in this kind of a situation when we are not sure what is likely to be the kind of direction that is going to happen in this particular month. Of course our intention is to do better CASA and improve the NIM. The second issue is that, I think over a matter of 6 to 7 months definitely interest rate has to stabilize. I do not think it can go on increasing at the current rate. So probably the latter half of the year interest rate would be somewhat better that is what I expect.

Amit Ganatra Second thing was on the margin guidance. Now previous quarter end and during the conference call, you basically mention that you are talking about 15 to 20 bps kind of fall in margins but that does not seem to happen at least this quarter. So does that mean the next quarter the margins will fall?

Murali Natrajan My team reminded me for the last three quarters I have been saying that NIMs would drop by 20-30 basis points and it has not happened. It is the kind of situation for me that, I have to deal with it, but the way I see it is that the Cost of Fund keeps on increasing as you have seen. You have the chart in front of you and we have been able to increase the Base Rate. Now many banks have already increased the Base Rate to 10.25%. Some of the Public Sector Banks have raised 10.2% to 10.5%, we have not done so. So I am being a little bit conservative, saying that if we are not able to pass on the increased rate than definitely there would be a dip in NIM. But I do not see the NIM to be, I mean I don't believe that we are planning to operate at a 2.8% NIM always because of our CASA focus and all, we should do better. But near-term NIM does definitely look challenging.

Amit Ganatra And the third thing was on the slippage. Now this quarter if you look at the additional slippage that has happened, although you are basically attributing large portions of that to the two corporate accounts but if you compare this slippage performance as compared to last full year, last full year of the gross slippage is only 1.5% for the full year and this year basically first-quarter itself its annualized rate is 3.3%, so this is the significant deterioration as compared to entire last year.

Murali Natrajan Do not put it like that, in number it might look like that. I have two Corporate accounts of approximately Rs. 15 and Rs. 12 crore, that have slipped. These are accounts which were looking stress for the last almost 18 months or so, we have been managing these accounts. One of these account we are confident of resolving it in the coming 3 to 4 months, the other one, the collection process is on. Whereas the bulk of the portfolio where we concentrate which is MSME, SME and Retail Mortgages, we are in pretty good shape.

Amit Ganatra Right, but Corporate still is almost 24% of the portfolio?

Murali Natrajan That is because, see it not from a percentage point of view, see it from, how the absolute amount has been in corporate and I will take you to page 17. If you see page 17, from Rs. 1,845 crore we have brought it down to something like Rs. 1,000 crore and we don't expect this number to go beyond this current level. So as the total portfolio increases, Corporate would look small. If you see the last quarter, Corporate was at about 26 odd percent.

Amit Ganatra So, but the concern is more on the chunkiness or the absolute, for example only 2 accounts deteriorated the slippage ratios very sharply. So maybe the size might be coming down or the percentage might be coming down but any further slippage from this basically can hamper the entire full year projections basically in terms of ROAs?

Murali Natrajan That is always the risk with Corporate accounts and that is the reason we do not focus on Corporates. At the same time there are existing customers, many of them have exited; many of them have reduced the exposure. So, what we are doing is, we are building up the rest of the businesses and simultaneously kind of reducing the reliance on corporate. So in this process, we don't wish any of the account to slip but it does happen in the corporate world.

Amit Ganatra No, but for example and for these 2 accounts you said that they were under stress last 18 months but now looking at your current portfolio, do you think that there are any further stress, large ticket stress basically existing in this portfolio?

Murali Natrajan Some accounts do come to stress and get out of stress, especially when there are Corporate account who take their working capital money and do some expansion plan they come under the liquidity crunch. Some of the Corporates have not been able to raise Capital on time so therefore, they have been under stress. Looking at the portfolio, I do not see any but looking at the way corporate business does, it does happen once in a while that some Corporate does come into a stress.

Amit Ganatra And your housing as a percentage of total has gone up significantly.

Murali Natrajan Not housing? Mortgages.

Amit Ganatra Yeah, Mortgages.

Murali Natrajan Mortgages, we have two parts, one is, Loans against Property which is a business loan that we give. It is an existing property and this loan is given to the customer at about 60% to 70% LTV, Home Loans are given at 80% type of LTV.

Amit Ganatra But wanted to know, have you acquired any portfolio this quarter or it's all organic?

Murali Natrajan Some portfolio acquisition may have happened but it is like more as a business as usual type of acquisitions. But I am confident; most of it is organic growth.

Moderator Thank you. The next question is from the line of Amey Sathey from JM Financial. Please go ahead.

Amey Sathey Thanks for taking my question. One question is on employee cost. Is it safe to assume that Rs. 30 crore of employee cost per quarter will continue for this year?

Murali Natrajan It is I think, Rs. 29 crore odd, it would be in that range except I have to add another 60-70 people in the new branches but that will have a calendar effect, I mean, I am not adding all of them in one month. So over a period of time we will add 60-70 people. Regarding the other operating expenses, we are confident that even if we put these 10 branches, much of it would be funded from efficiencies of the existing operating incomes.

Amey Sathey So, in that also Rs. 28 crore is likely to continued?

Murali Natrajan It will be in that Rs. 28-29 crore range, that is what we tend to aim.

Amey Sathey And second question on the Cost of Funds, like do you expect another 30 bps increase in Cost of Funds, year onwards or?

Murali Natrajan That has always been a very difficult question. I think it will be another 50 basis points.

Amey Sathey Okay and you also raised your PLR in May 27, I think. Has the full impact been reflected in your yield on advances?

Murali Natrajan In June we have a full impact of the increase for the quarter. But for that matter even the Cost of Funds has increased only step-by-step.

Amey Sathey Can I get the breakup between current and saving accounts?

Murali Natrajan Saving is Rs. 1,143 crore, Current is Rs. 849 crore.

Amit Ganatra Okay and the last question that the 2 accounts that you have slipped actually, where loans were given under your regime or it was under the early management?

Murali Natrajan We have not seen any slippages of any new account in the last 2 years that we have disbursed. But these are customers who were at a higher exposure level in the past and in the last two years we have reduced the exposures substantially. I do not look at my regime, previous regime and all, I own the entire portfolio, and we want to make sure that the entire portfolio is managed well. After two years also I can't keep saying previous regime, this regime and all these things.

Moderator Thank you. Ladies and gentlemen we will now take the last question from the line of Jasmina from ING Investments. Please go ahead.

Jasmina Hi, this is Jasmina here. Sir, I have a question on the Bank strategy for the next 2 years. What kind of Loan mix we are looking at and what kind of growth do we see in our fee based income because I have seen our commission exchange business has remained muted and what kind of cost to income ratio we are targeting? If you see our overall Retail Loan proportion in the last two years has come down from 40% to 34%, where Mortgage Loan portion has increased significantly from 8% to 30%. And even SME and MSME have jumped to 25% from 14%. So in view of the change which has happened in the last two years, what kind of loan mix we are looking at, in the next two years and what impact that will have on our net interest margins?

Murali Natrajan Barring this difficult period that we have seen in terms of the interest rate environment. Our target is to maintain our NIM at 3% plus, primarily because we want to have CASA of above 30% and if you see many quarters since 2009, we have always maintained CASA above 30%. The other thing is that, with the same number of branches, we have been able to grow CASA by Rs. 500 crore in last 2 years. Our aim is to take with the same number of branches; CASA to a level of Rs. 35 crore per branch in 2 to 3 years time and that is where we are making the investment, since December we have been making those investments.

What is the strategy of the Bank for advances, our main target is, self-employed customer. So 70% of our loans would be to self-employed customers. What we are targeting is to have Retail Mortgages, so when you say Retail Mortgages is basically Retail we do. We do not do builder financing and all these things. Our portfolio must be less than maybe Rs.30 crore for any development finance and things like that, so we do only Retail Mortgages, that is the area our focus. There we have two products, one is, Home Loans, another is Loan against Property. The split would be anywhere between 60-40 type. The other area of focus for us is, SME and Micro SME, again you see in page 17, how we have grown these two books. We give working capital advances and term loans to these customers on a secured basis. In 2 to 3 years time, what we would like to see and that is where we are working towards it, is that we would like to see mortgages about 25% to 26% of the total book and SME, Micro SME at about 40 odd percent. So 65% of the book would consist of these two products and why we are doing it because we want to reduce our large ticket exposures, so that business becomes lot more predictable because when you have Corporate loan even if one account goes NPA then it kind of puts pressure on the profits of that particular quarter. That is precisely what we want to avoid and we have been doing that, if you see we have reduced our reliance on Corporate and increase our reliance on SME and Micro SME in the last couple of years. So the composition of the book would be approximately 40% in SME, Micro SME and 20% to 25% in Mortgages, the balance would be in priority sectors lending and Corporate and the rest of it. NIM is targeted at about 3%. To do a great job in CASA, we might even do better than that but I think 3% is what we think we could do.

Jasmina And what is your outlook on the fee-based income?

Murali Natrajan Fee-based income, we have done a lot of granular work on the fee-based income in terms of training people for teaching Trade, Bank Assurance, General Insurance and even on Wealth Management. We have approximately about 200 IRDA certified people in our Bank and we are increasing that number. So the strategy is to have granular fees by cross selling to our CASA and loan customers. The fee has been static primarily because there have been challenges in terms of the bank assurance commission rates coming down in the last one year, whereas what we see that we have made it up in terms of volumes. So we think that we can grow fees by about 10% to 15% every year and the idea is that in three-year's time at least 70%-80% of our total cost should be met with fees.

Jasmina And what is your targeted cost to income ratio?

Murali Natrajan If you have got a highly retail and SME business which is what we are planning to be, we don't think our cost income ratio can be better than 55%. The reason why cost income ratio is high is because we have a small Balance Sheet and wherever we have added costs in the last two years is only frontline cost. Let me just give you some slight history on this cost. In 2009 March as we ended our cost annually was Rs. 242 crore. We reduced that to Rs. 201 crore in 2009-10, we increased that to Rs. 215 crore in 2010-11 and we probably will end up at about Rs. 235 or Rs. 236 crore this year, which means we have recycled the entire cost to create absolutely fresh set of businesses. And more importantly we moved away from high-risk business like Retail Personal Loans etc. to more secured business like Retail Mortgages, SME and Micro SMEs. So I think that, if we are able to grow our Balance Sheet consistently, we don't need to make any investments and technology or premises and all these things, of course we will have some branches coming in as in when we will get approval. We should be able to target 55%-57% type of cost income ratio in 2 to 3 years time.

Jasmina Sir, what will lead to reduction in cost to income ratio?

Murali Natrajan Growth in Balance Sheet and income because, that's exactly where we are focusing on. We have the capacity to grow the Balance Sheet and that is where we are focusing on growing. So our only investment that is required is for frontline sales people, the other fixed investment we already have.

Jasmina Basically, improvement is not coming from reduction in cost. It will come from improvement in the income?

Murali Natrajan No, we don't want to reduce the cost in absolute any further which is all I just mentioned you just a minute ago, that we reduced the cost from Rs. 242 crore to Rs. 201 crore and started actually building up new businesses like MSME, SME, Retail Mortgages with the same cost. So in a cost sense, we are still lower than what total cost was there two years ago.

Jasmina Right and on the Other Income side you have a line item called miscellaneous income, whereby in the entire FY 11 we did about Rs. 10 crore but in this quarter it was around Rs. 1 crore and year-on-year also it has come down from Rs. 4 crore to Rs. 1 crore. So what is the source of this income and why it has declined so sharply?

Murali Natrajan I do not have the details of that with me here but all I can say is that I will check. This is your talking about Q1 2010-11, right?

Jasmina Yeah, Q1 FY11 it was Rs. 4 crore, it is there in your presentation.

Murali Natrajan Yeah, Rs. 4 crore in Q1 2010-11. Okay, I am just guessing but I will come back to you through Bharat. Probably some aggregation of some income in the previous year that would have got recognized in the 1st Quarter but other than that I can't think of anything else on that. But you see, Q4 2010-11 at Rs. 1.22 crore and Rs. 1 crore in the current year but that quarter I am not very sure, sorry about that.

Moderator Thank you. I would now like to hand the floor back to the management for closing comments. Please go ahead sir.

Murali Natrajan Thank you for listening in and if you have any further questions, please feel free to write to us and any of you would like to meet us, we are happy to meet with you, so please do write to us.

Moderator Thank you. Ladies and gentlemen on behalf of DCB Bank that concludes this conference call.