"Kotak Mahindra Bank Q2FY23 Earnings Conference Call"

October 22, 2022

MANAGEMENT:	**MR. UDAY KOTAK – MANAGING DIRECTOR & CEO** **MR. DIPAK GUPTA – JOINT MANAGING DIRECTOR** **MR. KVS MANIAN – WHOLE TIME DIRECTOR** **MR. GAURANG SHAH – WHOLE TIME DIRECTOR** **MR. JAIMIN BHATT – GROUP PRESIDENT & GROUP CFO** **MS. SHANTI EKAMBARAM – GROUP PRESIDENT & WHOLE TIME DIRECTOR DESIGNATE** **MR. VIRAT DIWANJI- GROUP PRESIDENT & HEAD CONSUMER BANK** **MR. JAIDEEP HANSRAJ – MANAGING DIRECTOR & CEO, KOTAK SECURITIES** **MR. NILESH SHAH – MANAGING DIRECTOR, KOTAK MAHINDRA ASSET MANAGEMENT CO. LTD.** **MR. PAUL PARAMBI – GROUP PRESIDENT & CHIEF RISK OFFICER** **MS. OISHARYA DAS- GROUP PRESIDENT & CEO- KOTAK PRIVATE BANKING**

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Moderator: Ladies and gentlemen, good day and welcome to the Kotak Mahindra Bank's Q2FY23 Earnings Conference Call. As a reminder, all participant lines will be in 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. Uday Kotak. Thank you, and over to you, sir.

Uday Kotak: Good afternoon, friends, and first of all, wish all of you a very Happy Dhanteras and a wonderful Diwali.

As we look at Kotak Mahindra Bank's second quarter numbers, I would like to first start by saying that we are in one of the most amazingly benign credit cycles I've seen for a long time. And it is just truly amazing how the credit cycle is going. And I hope that this cycle continues as we go forward despite the increasing interest rate scenario as we move forward.

Talking specifically about Kotak Bank, you would have seen our credit slippages numbers as well as NPAs and credit costs are continuing to be extremely low. And we do believe at least at this stage of the cycle, we are not seeing any potential stress coming onto the balance sheet. We are of course very well adequately covered and prudentially underwritten in terms of the quality of our book.

On the credit growth, we are seeing both in the marketplace and at the Bank a significant growth in the commercial vehicles, in the tractors, in unsecured retail, microfinance, MSME, and even the home loan product, a continuing growth in that cycle, which is enabling us to continue with a loan growth which is quite solid.

We are also seeing an improvement in our mix of unsecured retail, which includes all of unsecured retail plus microfinance, which has now moved to about 8.5% of our total lending book.

You may recollect at the last call I'd mentioned we are looking at this number in due course going to around the mid-teens numbers, which is where we are comfortable going to.

Another very interesting aspect is that as interest rates move up, the nature of the book which we have, is about 70% of the book is a floating rate book and out of the balance 30%, about 10% of the book is less than one year.

The investment book, which is our government securities and bond book, has a duration of about one year, and therefore much less exposed to pricing and MTM risks as we go forward, though we carry about 64% of our book, which is mark-to-market book and HTM book is around 35% of our total investment book.

On the deposits side, we've had the historical advantage of a high CASA ratio, which as you know about a year ago was around the 60% mark. And as interest rates have tightened, we have seen some bleed particularly in the savings account book mainly on account of our high networth and affluent customer base, many of whom have moved their money out of the savings deposit rate to liquid and fixed income instruments which are offering short-term higher rates. We believe this bleed was inevitable because of the nature of the high networth customers who has now started getting much higher returns at the short end. At the same time, we are very closely monitoring and measuring our granular SA book, particularly, SA balances up to Rs.10 lakhs and which is showing continuing growth through this period.

Our term deposits which is other than CA and SA, has grown pretty well. And our overall non-CA and SA deposits now are growing at about 20% p.a.

On the current account side again, our granular growth is quite good. We have grown about 13% YoY despite the fact that some of the balances in the custody business have dropped on account of reduction of floats left by foreign portfolio investors in their custody accounts. So, CA story is still reasonable. On the SA story, the higher networth customers have withdrawn some of the monies for significantly higher rates compared to the savings account, but the granular SA growth up to 10 lakhs continues to be pretty good.

On the deposit focus, as I mentioned, there's a very high focus as we go forward. And as you are aware, we have now got the government agency business. We were amongst the later round of private sector Banks which got approval in this round compared to some of the other public sector and the private sector Banks who have been in the agency business for a long time. We are seeing very good traction with our customers around the agency business, payments and flows. We believe that in turn will lead to a granular growth in our CA and SA balances as the government business picks up and we're looking forward to a very high focus on that in addition to the salaried customer in terms of the deposit strategy.

One of the other factors if you look at with reference to many of our subsidiaries, they all continue to be very robust. Some of them have felt the pressure of the slowdown in the capital markets, which has impacted their earnings numbers relative to what they were in the same period last year, which was a bonanza time for capital markets businesses.

All in all, I think, we are seeing a decent growth in profitability, a very, very strong and robust balance sheet, high capital adequacy (consolidated) in excess of 23%, which also gives us room to be much bolder in terms of our strategy on the different segments of our business as we go forward.

I would here also like to mention that we are continuing to focus on new opportunities in some of the segments including the alternate assets businesses, which we plan to grow pretty rapidly as we go forward.

With that, I will now hand over to Jaimin Bhatt to take you through the numbers.

Jaimin Bhatt: Thank you, Uday. Let me take the financial numbers for the consolidated which is for Q2FY23. We closed this quarter with a post-tax profit of Rs.3,608 crore which is compared to Rs.2,989 crore in the same quarter last year. If I look at a QoQ basis, we have a growth of 31% (not annualized) as we have closed previous quarter at 2,755.

Our customer assets at the consolidated level was up 24% at Rs.3,57,000 crore. At the consol level, our ROA at 2.61% as against 2.36% which was for the year ago. And ROE at the consolidated level at 14.1 % and for the half year at 12.7%. The Bank contributed 72% of our overall profits for this quarter at Rs.2,581 crore.

Kotak Prime brought in profit of Rs.222 crore as against Rs.240 crore last year and Rs.157 crore in the previous quarter, whereas the other NBFC, Kotak Investments brought in Rs.78 crore post tax as against Rs.89 crore.

For Q2 last year, both the NBFCs had some treasury gains whereas for KMP in the previous quarter, which is Q1 of this year, we had taken a one-time hit on accounting change of pre-tax Rs.111 crore.

Our microfinance business correspondent entity which is BSS, clocked a post-tax profit of Rs.70 crore this quarter versus Rs.56 crore in the immediately preceding quarter and Rs.8 crore in Q2 last year.

The overall lending related entities therefore brought in about Rs.2,958 crore of the post-tax profit which is 25% growth over the same period last year.

As Uday mentioned, we had a subdued capital market this time, and the broking and investment banking subsidiaries therefore had drop in profits; Rs.246 crore this quarter as against Rs.301 crore last year's Q2.

Kotak Securities though increased its market share both in the overall market to 5.1% and 11.2% in the cash market.

The life insurance entity at the shareholder level improved its post-tax profit from Rs.155 crore last year Q2 to Rs.270 crore this quarter, whereas the domestic mutual fund entities brought in Rs.106 crore, which is about the same level as last quarter.

Overall capital and reserves at Rs.1,03,000 crore, whereas our capital adequacy both continue to be healthy at both the capital adequacy and the CET-1 levels.

Capital at the Bank at Rs.77,000 crore and both the NBFCs continue to have capital adequacy of in excess of 30%.

Kotak Securities and the Life Insurance Company again having healthy capital. The Life Insurance Company with a solvency ratio of 2.79.

The Bank standalone profits as I mentioned was Rs.2,581 crore, 27% higher than same period last year. If I compared to the immediately preceding quarter, that's a 25% growth, which is not annualized. Thanks largely due to the MTM hit, which we had taken in Q1.

The NII growth for the Bank is at 27% for a YoY and 9% on a QoQ basis. We are seeing advances book at the Bank grew 25% YoY and we close at Rs.2,94,000 crore, along with the great substitutes this would get to Rs.3,21,000 crore. The retail unsecured book, as Uday mentioned, we are now at 8.7% of the advances. We've seen the NIM clocking to 5.17% this quarter as against 4.5% a year ago. And as Uday mentioned, 69% of our loans are on floating rates.

On fees and services, we saw a growth of 24% on a YoY basis while the syndication income saw a small drop. The general banking fees grew 37% on a YoY basis.

As I indicated in Q1, we had taken a hit of Rs.857 crore on account of MTM hits. For Q2, this is a much smaller number at Rs.63 crore. And our HTM book continues to be at a low 36% of our total investment book. Our modified duration also continues to be low at 1.05 years.

In Q1, we had some negative cost which is a writeback of cost on our retirals thanks to a rising interest rates, things have now normalized and we've also seen a very sharp rise in DA in this quarter, resultantly on a QoQ basis we see a rise in the employee cost.

Non-employee cost again, we've seen a growth as we talked in the previous quarters as we push for growth both on the asset side and the liability side.

We closed this quarter with a total customer base of 36.6 million.

At operating profit level, we were therefore 14% higher than the same period last year and 28% higher than the immediately preceding quarter.

We continue to look at COVID and restructuring provisions on the same principles as we've done earlier. And we've seen therefore a small release of our COVID provision for this quarter.

Our credit cost for this quarter was at 26 bps which includes provisioning on account of standard assets as the book size has gone up.

GNPA continues to be at lower levels. Total absolute number at Rs.6,200 crore compared to Rs.7,600 crore which we had a year ago. And the GNPA percentage at 2.08 as against 3.19 a year ago.

With a PCR now of 74%, our NNPA at 0.55% as against 1.1% last year.

Slippages again have been pretty low at Rs.983 crore, which includes about Rs.330 crore which actually got upgraded during the same quarter.

Our restructured advances either under COVID or MSME together account for 0.34% of our advances book. And our SMA-II which is for exposures over Rs.5 crore continuing to be low at Rs.119 crore.

CASA at 56% and capital adequacy which including the profits for the half year at 22.6% and the CET-1 itself at 21.5% at the Bank level.

So, that's broadly what we did at the Bank. I would request Manian to take you through the Wholesale banking.

KVS Manian: Hi, everyone. Good afternoon. Let me take you through the wholesale banking business. As we usually see, we'll see it in two parts

Overall, in the SME segment, I think the growth remained robust; YoY 25% and QoQ even better at 9%. We continue to focus on this segment as a growth area. We've been very successful with acquiring New-to-Bank customers in this area. And the growth in the NTBs is even faster than what the book appears to be. We are also seeing good demand here for capacity creation in the form of term loans, but of course these get drawn over a period of time. We've also expanded our footprint in this segment by adding seven new locations in the last half year, and we will continue doing that and go to a few more tier-two locations, and we are seeing good demand in these locations.

On the corporate book itself, while, of course, advances look close to flat, as we usually do, we need to see that in conjunction with credit substitutes. We have a fair amount of irrationality in pricing here in this segment, and we remain choosy.

We continue to optimize our PSL costs and ROE by suitable mix of credit substitutes as well as loans and also rediscounting bills where necessary. and also by not taking on some of the mispriced assets on our balance sheet.

We continue to build our franchise here and believe that we have the right access and good visibility of all transactions that happen. And we are able to choose what we think suits our risk/return matrices.

In the large conglomerate segment where the price competition is even higher, the redeeming feature is that they are better-rated and we are able to substitute loans through credit substitutes.

We are seeing opportunities to grow in the mid-corporate segment where we can manage our profitability and risks much better and we intend to focus on that segment.

The CRE part of the business has also remained stable. Of course, the residential demand, as you all know, has been extremely robust. But what that results in is significant prepayment of the project loans that we have done, putting pressure on the growth of the book.

On the commercial side of real estate, I think the LRD pricing remains irrational and we have relatively stayed out of this market.

Overall, our philosophy of making sure that we earn the right risk adjusted return remains. Our DCM fees have moderated a bit this year, but all other fees continue to grow at a robust pace.

Our portfolio quality has held up quite well. SMAs as well as NPAs remain low, the ECGLS part of the portfolio also remains as robust as the rest of the portfolio.

Our digital and tech initiatives continue to gain momentum. We have upgraded our technical architecture and stack on the trade, cash and other payment platforms.

The integrated banking portal is gaining good traction and adoption by our customers. These help us in gaining better share of the transaction banking business.

As Uday briefly mentioned, our non-custody CA growth remains robust. Even in custody, our domestic custody seems to be growing reasonably, of course FPI custody is where the negative growth is happening.

Overall, we continue to gain momentum and traction in our transaction banking business.

We have also launched an internal project to reengineer and optimize our processes to achieve better customer outcomes as well as productivity. That's all I had to say on the corporate side.

Now, I hand it over to Shanti to take the Commercial Bank?

Shanti Ekambaram: Thank you, Manian. The commercial vehicles industry has seen strong demand in Q2. Goods freight demand was strong and better availability of return load, led to improved operator economics. The bus segment has also bounced back and is doing well across all verticals.

For Kotak, the business has seen strong growth in disbursement and we grew our SOH 26% YoY, helping us improve our market share across all segments of commercial vehicles. We will look to build our book with focus on risk adjusted return.

Collection efficiency continues to see improved level for the segment.

On construction equipment industry:

After a muted July and August, there was a sharp uptick in September for the construction equipment industry. Demand for road equipments has been a laggard, while all other segments showed an uptick. Customers have reported better utilization of their equipments and better cash flow. We saw good disbursements in this business and SOH grew 24% YoY and we will focus to grow our market share in geographical presence in the segment. Collections again have remained very stable during this period.

On Tractor Finance:

The tractor industry has seen an uptick in demand owing to better cash flows of last harvest and pickup of commercial deployment. Also, customers in this segment continue to receive good government support. We have grown our disbursement strongly across both new and used tractor financing and improved our market share in the segment. Given the good monsoon, robust cash flows and outlook for the industry, which continues to look good, we continue to remain focused on rural customers in the farmer segment in particular, with a focus to deepen our distribution and improve our market share.

Collection efficiencies have improved and are better than pre-pandemic levels. Our SOH has grown 24%.

Our microfinance business continues its growth momentum in Q2. We have almost doubled our portfolio year-on-year. The collection efficiencies in this business climbed to reach the pre-pandemic levels indicating the ability of microfinance customers to service their obligations. The focus of this business will continue to be in rural and semi-urban markets and primarily borrowers in the agri, allied agri and micro business segment. We will continue our focus on a high growth strategy in this segment.

Agri SME:

In the food and agro processing space, commodity prices had peaked in Q1 and due to which demand at that time was good. With a drop in the commodity prices, we have seen a little reduction in the working capital in the commodity space. The cash flow of the customers, however, is quite comfortable and the CAPEX investments in this segment are seeing an uptick primarily in the processing capacity and for augmenting the agri infrastructure, which is warehouse, cold storage, supply chain, etc., We continue to grow at a healthy pace in this business including acquisition of NTB customers. With good monsoons, kharif arrival is also expected to be good. Hence, we expect demand for credit also to remain strong in this business and we will continue to deepen widened distribution and grow in this space.

I now request Virat to take you through the Consumer Bank Business Highlights.

Virat Diwanji: Thanks, Shanti. I will start with consumer assets. We continued our robust growth trajectory in consumer assets lending in this quarter clocking YoY growth of about 39%. This has helped us to gain market share in couple of our product lines in spite of rising interest rates and thereby EMI demand for home loan is still holding. Even the demand for loan against property was showing positive signs. Our mortgage business lending grew by about 40% on YoY basis.

We had yet another good quarter on credit cards with an acquisition at over 7.25 lakh cards in the quarter. Spends using the card saw a robust growth this quarter showing 93% growth on YoY basis. Bulk of the sourcing continues to be from existing bank customers. Our co-brand partnership with PVR and Indigo cards are also yielding good volumes. This quarter, we also went live with our assisted digital journey for New to Bank customers enabled with soft decision upfront coupled with biometric KYC. Overall, credit card advances grew by about 16% on QoQ basis.

Demand for unsecured retail consumer loans, continue to be vibrant and we grew our book by about 80% on YoY basis. We have scaled up our customer acquisition in both the traditional and data-led digital space in this business. Consumption finance or EMI business is a growing space for us and we did six lakh units plus last quarter. As you know, this business has presence at retail outlets and on online stores. These numbers are over and above our EMI business in credit cards.

Now, we'll go to business banking assets. We witnessed an increase in credit demand aided by better utilization and increase in CAPEX demand from select pockets across retail business banking sector. We continue to grow and gain market share in MSME space by expanding distribution footprint, widening distribution channels and technology enablement with ultimate aim of being holistic banker to this segment of customers.

Overall, collections is well in control with no apparent diversion from the past and we continue to seek our risk weighted returns across customer segments.

Now, we'll go to liabilities, the upward revision of the interest rate cycle during the first half of the current financial year have rendered attractiveness to the otherwise conservative investment avenues like Term Deposits and Liquid Funds for HNI customers. As the gap between the interest rate on SA and returns on liquid funds widen, some bulk SA deposits have moved to liquid funds. However, the Bank has observed good growth in the granular savings deposit book, which denotes the core strength of a saving franchise. The existing granular savings book which is below Rs.10 lakhs, has shown a healthy growth, contributed by deeper customer engagement efforts and enhanced conversion quality via delivery of right fit solutions.

With enhanced focus on salaried segment, we are hopeful to continue to build our granular SA book even stronger.

We have also seen good traction in our agency business and lot of retail customers have started using our platform to make Customs Duty, GST and Taxes. This will certainly help us build flows and balances in our CASA accounts. Government business is also a key focus area for us.

During this quarter, we launched a couple of savings products aimed at retail customers, which encourages them to use Kotak account more frequently.

As we aligned the rates on the term deposits to market rates, we were successful in locking the outflows from the savings account deposit for a longer duration term deposit. Retail term deposit growth trajectory change to show a growth of around 16% on YoY basis.

Continuing with our focus on granular buildup of low cost and stable deposit, we launched a new offering for our retail merchant segment, called- Merchant One Account, which aims at digitizing merchants business and has payment collection solutions bundled with the current account. The initial response to this offering has been extremely encouraging. We also launched a new pay by SMS or link facility for merchants who are part of Kotak.biz ecosystem. The new features allows merchants an additional mode of payment collection through a link sent on SMS to the customers.

I will now hand it over to Dipak for Digital.

Dipak Gupta: Thanks, Virat. On the technology side, you would have heard that Milind Nagnur has joined us as our CTO. Milind comes with a very strong technology background coupled with global banking experience.

On the technology side, the key focus areas, which we've outlined in the near term really are building resiliency. As you know, the customer base grows and the technology pieces become more complex, it is extremely important to build resiliency. What we are finding really is, ensuring that your systems and technology, particularly the customer-facing systems are focused, it is very important for them to be resilient to attract customer and customer journeys really.

The second piece on the technology side which we're focusing on is creating scale and capacity for meeting future growth. Some of the areas particularly on the payment side, which is really on the UPI piece, we're seeing growth multiple times within a quarter itself. And it's extremely important to build scale and capacity in these areas. And similarly, transitioning to the cloud is a key focus area for us. Over the next, six to twelve months, we expect a large part of our technology systems to move to the cloud, except probably the core banking piece really.

And finally, on the technology side, we want to significantly enhance all our customer journeys, whether it is acquisition journeys, it is Do-It-Yourself or assisted journeys, and all customer engagements. And a lot of the activity which you see really, what we've been building, and we propose to build, are essentially to enhance all of these Do-It-Yourself journeys.

On the digital channel, a lot of effort has really gone into ensuring that the UPI-related pieces are stable and meet the increasing requirements of customers on that front.

Our mobile banking app still has a very healthy rating on the iOS side, probably amongst the best in the industry, and a reasonable rating also on the Android side.

On the merchant and the corporate side, you heard what Virat mentioned about building digital update and Manian touched upon the transaction banking technology which we are putting in place through FYN. We've seen very significant transaction throughputs on both these counts really.

Some of the digital highlights are mentioned out there. What we're really finding is close to 98% of our SA transaction volumes were in digital and close to about 95% of our accounts are now opened entirely digital.

We've been investing and participating actively on the India stack and various components of that. We've been the first Bank to go-live on OCEN. Account aggregator is now pretty much a practice proposition. We've recently experimented with and have been the first in the industry to launch face authentication. This is a new piece which offers an additional mode of authentication to customers. That's all on the technology side.

I'll now move on to Kotak Prime. Just a quick update on it. What we are finding really is the car finance market is growing pretty comfortably close to 18%-20% growth on the volume side, but interestingly, the value growth has been significantly higher, and one expects the value growth to be close to about 25% during the course of this year.

Some interesting trends what we are finding really is while the demand for the lower end cars is sort of stable, we find a lot of dealer inventory building up at the lower end, but the mid and upper end cars are moving at a pretty healthy pace. In fact, the mid-range cars which is really the 10-12 lakhs range now seems to have become the choice of a first time car buyer now really, and that's an interesting change, which we really are seeing.

On KMP's performance, we now have a customer asset base of over Rs.20,000 crore. Jaimin talked about our profit after tax being Rs.222 crore in this quarter, which is up significantly from the previous quarter primarily because last quarter we made a significant accounting policy change on brokerage.

That's all from my side, I'll hand it over to Gaurang to take you through the Insurance.

Gaurang Shah: Thanks, Dipak and good afternoon. For the Q2, we posted profit after tax of Rs.270 crore, which showed growth of 74% over last year and on QoQ at 9%.

Gross written premium for the quarter was 11.5% YoY, reaching Rs.3,250 crore premium.

Individual new business APE for Q2 grew by 13.7% where private industry growth was 7%. So, I think more or less the premiums are getting more normalized as the base effect is waning.

The good story was on protection. The protection premium was 54.1% up compared to the previous year. And this is also a combination of more life covered as well as higher rate of protection premium which is getting charged, which also contributes to a certain extent to the increased profitability.

The AUM showed the growth of 13.8% to reaching Rs.53,785 crore. The death claims also have now normalized and to pre-COVID levels. In Q2FY23, death claims, net of reinsurance was Rs.275 crore, exactly half of what we posted in the previous year.

Our networth has now reached Rs.4,792 crore, giving us a very strong solvency ratio of 2.79.

Now, I hand it over to Jaideep to take the presentation forward.

Jaideep Hansraj: Thank you, Gaurang. The total revenue for Kotak Securities for the quarter ending September '22 was Rs.631 crore. This is comparable to Rs.613 crore in the corresponding quarter last year and the number for the previous quarter was Rs.616 crore. This resulted in a PBT for this quarter of Rs.298 crore compared to Rs.325 crore in the corresponding quarter last year and Rs.291 crore for the previous quarter.

The PAT for Q2 of '23 is Rs.224 crore compared to Rs.243 crore for Q2 of '22 and Rs.219 crore for the quarter ending 30th June '22.

The cash market share of Kotak Securities has been seeing a steady increase and has reached 11.2% versus 11% in the corresponding quarter last year and 10.4% in the previous quarter.

The options volumes have been driving the market volume significantly. The ADV for the total volume alone has reached 64.7 lakh crore, of which options is 63.47 lakh crore. This is compared to 30.4 lakh crore in the same period last year, which is more than a 2x increase just in options alone.

There have been significant upticks in our digital journey. We launched our state-of-the-art trading platform, Kotak Neo sometime in the last quarter. And in a short span of time, a large percentage of daily volume are happening there. The plan is to shift majority of our trading volumes or all our trading volumes on to Neo in the next nine to twelve months.

We launched a Smart Payoff Analyzer for option traders, which has helped them significantly and we've seen a lot of customers move because of this payoff analyzer which we launched in the last quarter.

The share volume increase in mobile and web has seen a large increase in last year or so.

With this, I'll hand over to Nilesh for the Asset Management business.

Nilesh Shah: Thanks, Jaideep. Good evening, friends. Let me take you through our asset management business. Our total average AUM grew 5% year-on-year to Rs.2.84 trillion. Our equity average AUM despite market correction grew 6% QoQ to Rs.1.52 trillion. Our net equity market share is at 6.31%. Our SIP inflows for September '22 grew 26% year-on-year to Rs.7.8 billion. Our retail AUM stands at 53%. We continue to serve investor requirements by launching active as well as passive funds focused on local as well as offshore markets across debt, equity and commodities. Kotak Business Cycle fund collected Rs.2,266 crore during the NFO launch. Our profit after tax was flat at Rs.106 crore for September '22 quarter. Our total AUM across mutual fund PMS offshore, insurance and alternate assets, grew 2% year-on-year to Rs.3.90 trillion.

Our relationship value across wealth, priority and investment advisory grew 20% to Rs.5.54 trillion.

Moderator: We will now begin the question-and-answer session. We have the question from the line of Manish Shukla from Axis Capital. Please go ahead.

Manish Shukla: First question is, for the last couple of quarters again, we've seen credit substitutes start growing and today it's almost more than 9% of loans. I just wanted to get the thought process around the same given the rising rate environment and what would be the nature of these credit substitutes in terms of duration, etc.,

KVS Manian: The credit substitutes that we have built through this year are all relatively short term, less than one year kind of tenure instrument. And like I said, it helps us to optimize our returns in terms of PSL costs, risk and pricing. So, in better rated corporates, with lower tenure we prefer to do credit substitutes than loans.

Uday Kotak: And if I may add to what Manian said just on that point, we got to keep in mind that where we have done credit substitutes for a longer period, we have also done floating rate credit substitutes. So, therefore, we are not exposed to interest rate risk. And separately, we have disclosed our total duration of our investment book, which includes credit substitutes as about 1.05 years. So the total duration in that includes the credit subsidies duration.

Manish Shukla: Okay, that's clear thank you. Second Jaimin if you could help with TDs less than two crore which is how RBI defines retail ready, what would be the proportion of that?

Jaimin Bhatt: Sorry, I didn't get you.

Manish Shukla: TDs less than two crore, what would that be?

Jaimin Bhatt: That would be about 60% odd of our overall TDs.

Manish Shukla: And, the last question is that margins obviously are at a very high level now. How do we think about margin trajectory from here on because given the nature of the book considering that 80% is floating or less than one year, should we expect more room for margin expansion from here on?

Uday Kotak: We have to keep in mind that we are a very disciplined bank and we are focused on risk adjusted returns and at the same time we are focused on growth. And despite some denudation on our SA because of the high-net-worth individuals moving the SA, we are still at a healthy ratio of 56%. And in the absence of any decision to change rates, which obviously is always an open-ended question with reference to savings deposits, but in the absence of that change, you got to keep in mind that as of 30th September, 56% of our book is fixed rate or quasi fixed rate because CA at zero is a fixed rate book. And SA at current rates is a quasi-fixed rate book. So, what it does in terms of margins, because as we have also disclosed fully our repo rate or external benchmark rate lending book, our MCLR lending book, our short term book, we've given you all the data. Therefore, as an analyst, I'm sure you can do your homework and figure out what it means. It will be difficult for us at this stage to conclusively say from a NIM rate of around 5.2%, where we end. But keep in mind, I have also mentioned that our unsecured retail, which is a high yield book, which is currently about 8.7% and is growing faster than the rest of the book, you can put that also in the equation. But having said all that, I want to bring one caveat right at the top, we are probably in one of the most important Cinderella times of the credit cycle.

Now, you and I can debate whether that Cinderella time is 1PM in the afternoon, 7PM in the evening, 9PM. We can figure out the time of the day when it is Cinderella time and then take a call how long this positive credit cycle remains which is very closely linked to the terminal rates of interest and the external account situation of the country. Therefore, we will be guided by a lot of factors as we go about our underwriting business with a singular focus on risk adjusted returns. And at the same time, we can see it from our operating expenditure, we are investing and Dipak mentioned about it, continuing to invest heavily in technology and also growth of both the asset and liability business. So, whatever it cost, we will take those costs, even as the rate cycle, interest rate cycle, and the margin cycle looks at this stage pretty benign.

Moderator: Thank you. The next question is from the line of Rahul Jain. Seems like we lost the connection for Rahul Jain. We'll move to the next question from line of Saurabh from JP Morgan. Please go ahead.

Saurabh: Sir just three questions, the first is sir what will be the LCR for the quarter?

Paul Parambi: LCR is 119.1%, similar to last quarter.

Saurabh: Second sir you mentioned about this percentage of unsecured, is there a target you have in mind. And if you can also expand on what's happening with this microfinance it is growing very quickly.

Uday Kotak: First of all, I want to clarify very categorically that when we give you unsecured retail number of 8.7% that includes all unsecured retail including microfinance. So, microfinance is part of our 8.7% unsecured retail. We have given an indication at the last quarter that our current comfort based on the cycle is to move to around mid-teens. So, we are currently at 8.7%, so, we still see reasonable room for growth even as the overall book grows in terms of the mix and we will take a view based either on the cycle or once we reach closer to the mid-teens number, what percentage of the mix we want as unsecured retail including microfinance.

Saurabh: Okay. And fair to say microfinance is now a focus area because the way you are growing it?

Uday Kotak: It's a part of our overall mix. We are very clear that whether it is a sector, segment, customer, security, one of the most important factors in our planning for risk adjusted return is keeping an eye on concentration risk.

Saurabh: Understood sir. And sir last question, this NIM improvement which you have seen quarter-on-quarter is it possible to break down how much would have happened due to bad book re-pricing and how much would be related?

Jaimin Bhatt: NIM improvement is as Uday explained earlier on the back of repo, the mix change which is also happening on account of unsecured going up and a mix of all that.

Saurabh: But would it be possible to break down what will be due to the bad book and how much it to the mix?

Dipak Gupta: It is not easy Saurabh. But the mix impact at this stage is still low, because on the unsecured side the absolute increases are still small.

Uday Kotak: So, Saurabh the impact of unsecured retail is still absolute size of the book is 8.7% on the stock.

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

Rahul Jain: Just a couple of questions. First just talking about deposit growth you started raising rates from last quarter, perhaps a bit too early to see, the kind of momentum building up, but when should we start seeing the momentum building up across different pieces of granular deposits, if you can just throw some light on that?

Uday Kotak: Rahul first of all, very high focus on granular deposit in the early part of the call we mentioned about how on savings we've lost some money in the affluent and the high net worth segment particularly some of that moved to the liquid funds which now offer close to 6%, 5.75% to 6%. Therefore, high net worth individuals are more sensitive to it. But our core transaction customer base and balances below 10 lakhs have seen a healthy growth. And I will ask my colleague Virat who spoke about it and who heads the Consumer Bank to share how he sees that grow, Virat.

Virat Diwanji: Thanks. Look in terms of growing of the granular book, we have couple of plans in place. First, how do we make the customer engagement easy and as we engage with the customers; we expect the book to grow that is one part of it. The second thing is now we are trying to use the digital route to acquire customers and that will help us to acquire more customers in that sense. The third one as I had mentioned earlier is the salaried customer base and that's a learning from this COVID era that the salaried customer book is usually a steady book and hence we will go a little more focus on that to really build the salaried book. Obviously some help from the flows happening because of we becoming an agency bank and that will have a rub off on building up the balances within the retail customers. So, these are couple of things that we are doing just now which will help us to build the granular book.

Uday Kotak: Having said that Rahul, a bulk of our loss in SA as I mentioned is on, what I call as high networth lumpy SA balances. So, which obviously when we were running as I mentioned at a 60% plus CASA, that was a place where we would obviously be vulnerable in a sharp interest rate increase cycle, we think a lot of that lumpy money has moved in the last few months as interest rates have gone up. After that our CASA ratio is 56%, we believe that there is a continuing growth in the granular book in SA, our overall non-CA and non-SA deposit growth is 20%, as 60%+ of our term deposits is deposits below two crore. So, between granular SA, term deposits below two crore, focusing on customer segments, which is around the salaried customer, greater focus on government accounts, which gets an even bigger boost post agency business approvals and the agency business we actually started for example the tax collections on income tax only in September. So, we are still in very early days of agency business some of the larger peers have been in this business for 15-20 years or more and therefore we are in still very early days of these engagements. And therefore, our high focus is on granular growth some of the lumpy deposits and when I say lumpy, I'm talking about deposits in the five crore plus category, which used to keep a lot of money in that savings accounts with us. Thanks to a customer focused, wealth management division, a lot of that has also moved into liquid funds.

Rahul Jain: And is that phenomena by and large over when you see the behavior of these customers or?

Uday Kotak: We think a lot of the high-net-worth money, they don't wait Rahul you know that. If somebody has got 25 or 50 crore with us and he is earning 4% in the savings account and when you have a pretty good private banking business, the relationship managers would do what is right in the interest of the customers and liquid funds start giving 5.5% to 6%, you know where the money goes.

Rahul Jain: Yes. Thanks that is very useful Uday. Just moving on to the cost part. So, part of the increase in employee expenses as Jaimin explained was because of the DA, but even otherwise also, it appears quite chunky and even the non-employee expenses, I know would be a fair strategy for you to perhaps deploy some of these gains in capacity building. But if you just look at the branch increases that's again pretty, pretty less and I would sort of expect your argument would be the digital element growing. So, can you just help us understand where you are deploying these resources and branches which of course are becoming again very critical focus for larger peer banks, how do you approach that in the coming quarters?

Uday Kotak: Rahul the highest winner of incremental growth is Mr. Dipak Gupta, who's focused on the technology and digital functions, so he's taking the highest percentage growth between digital and technology costs. And, as you know we've added the new Chief Technology Officer, we have added a new Chief of Customer Experience. So, we are fundamentally and structurally changing how a bank is thinking on the technology front to a transformative mode. And maybe Dipak you want to talk a little bit on the whole technology transformation. And on the branch, we will continue to steadily add branches, we believe branches still continue to be important. Our view however is that the density requirements of branches compared to the past maybe less, therefore branches are still needed. But instead of being at a distance of 100 meters from your home I'm sure people can live with a branch which is half a kilometer or a kilometer from the home. So, that is continued steady increase in branches, not dramatic, more focused, also more focused on the current account customers, because interestingly we find the savings account customers are moving much more digitally compared to the current account customers and therefore technology is the place where we are putting the money. Dipak Gupta please.

Dipak Gupta: So, Rahul since Uday has talked about all the cost. All I can tell you is, the mobile today has become the largest branch. So, whether we add physical branch, infrastructure or no, the mobile and to some extent the net do take away a large part of the technology cost really so a large number of projects and investments going into that like I explained significant investments in do it yourself journeys and assisted journeys. But that's one part of the cost on the technology side, which you see out there. The other significant delta on the cost really is two sub parts. One is, if you see all the retail asset pieces, all of them have grown at a pretty healthy trot, there is a significant amount of upfront cost, which you take on a count of acquisition, and then there are direct variable cost for example cards, you see in a pretty healthy growth on the overall AUM on the cards, all of that requires you to keep spending continuously. So, those are direct variable costs of the growth in the AUM and of course all the assets pieces are like I said growing pretty well. And acquisition cost on those just hit you upfront. So, all those costs really are technically if you see more than anything else one-time cost, the regular cost, the increase really is on the employee side nowhere else.

Shanti Ekambaram: In addition to the retail asset businesses, I just want to add even 811 we have been growing aggressively month-on-month, and those acquisition cost are also upfront. So, they all add to what Dipak talked about the customer acquisition cost and growth cost.

Uday Kotak: And Rahul keep in mind, for the relative size of the branch network we've added 21 lakh customers in this quarter.

Rahul Jain: Got it. I just have a couple of more questions, but I just keep the last question, this one is the competition, given that everybody start benefiting on the margins, the margins are even increasing by 30- 40 basis point quarter-on-quarter, we've seen there's a PSU is taking a lead and passing that back to the customers, SBI launched that festival scheme of home loans, I think HDFC also responded, maybe if the environment remains like this for banks, the competition might inch up. So, when we are seeing growth all across the Board in your loan portfolio, which are the segments that will grow faster in the next couple of quarters, do you have anything in mind or you will be like, wherever the demand comes from meeting your risk return criteria you will keep growing, how are you thinking about the growth versus profitability?

Uday Kotak: Broadly, it will be driven by the risk return matrix. And that does not make us shy if we want to penetrate a particular segment to go aggressive on pricing. But if you look at this quarter Y-o-Y and Q-on-Q growth across different customer segments, you will get a pretty good idea where we are growing rapidly and pretty well. And some of the segments which were down for a long time has suddenly come alive, like the commercial vehicle segment. Commercial vehicle was at a very tough previous two years, but it has come back. So, we are very focused on where we think there is opportunity and where we think we can make reasonable margins, we are not necessarily focused on disproportionate margins. But if we get, and we are comfortable with our risk we will go ahead and take the volume, as long as we believe our ability to fund appropriately which is there very much and we think for us getting money is less of an issue, more is about the price of money even now if you look at our cost of funds calculation we are extremely competitive on cost of funds. But we like to make sure that, and Rahul you know this, as I said this is a wonderful Cinderella time only point is we don't know what time of the day it is. So, we are actually very conscious that this is still probably a little early in the Cinderella time, well before midnight, but we have to be ready that if and when that clock strikes we are in a good shape to be able to handle that time.

Rahul Jain: Absolutely, that's the reason I asked that question, the moment it strikes in the midnight you should be able to exit or maybe slow down this portfolio.

Uday Kotak: So, at this stage we don't think Cinderella time is like happening too soon. Now whether it is after a year or later, a lot of it depends also on what's happening around the world and also the external position of India, which is currently robust. But this is a fast changing world.

Moderator: Thank you. The next question is from the line of Prakhar Sharma from Jefferies. Please go ahead.

Prakhar Sharma: Sir, just two questions. One on the Treasury loss, last quarter you had a very big loss, roughly 800 crore and your duration is short generally about a year, so what we had seen generally is last quarter we saw 150 basis point rise in yield. And you had 800 crore of M2M loss, this quarter one-year bucket had still seen a 50 bps right. But your M2M losses, less than a 10th of what it was, so could you explain what's the reason for this?

Jaimin Bhatt: Prakhar that portfolio would have churned also, it's not that it was static for this period. So, the rates have changed, but you've also taken the portfolio some of that out and bought some new also during that period.

Prakhar Sharma: Would that be fair to say that, the fact that your deposit growth is slower and you sold investments to convert in practically?

Jaimin Bhatt: No, it is not linked, they are two independent things.

Prakhar Sharma: Got it. And just based on your experiences.

Jaimin Bhatt: One other thing, for some of the other portfolios which are there as part of this, where you have taken a mark to market negatives, some of that actually turned out to be better than what was there. So, you got a slight uptick on that.

Prakhar Sharma: Sure. And just based on your engagement with the customers, the HNI customers who basically move money around, in times like this is there a way you can convince them or whatever to keep hold more deposits or it's basically that you just hold tight during the cycle and when things normalized you get back?

Uday Kotak: I'll ask my Head of Private banking, Oisharya Das to explain how she is able to talk to her HNI, but the first principle she always tells me is, my customer comes first.

Oisharya Das: For all of us it's always the customer first and the right advice should go to the customer. So, there should be no conflict there. And we've always given that so. We are looking at this thing the customer base granularly and if interest rates are on the rise we will move customer money there. So, does that answer your question.

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

Kunal Shah: So, firstly, again with respect to deposits and that's across the system and that lagging the credit growth, but when do we see actually the action on pricing, because this has to come through from pricing as well. And people are still holding on to savings rate, deposit rates have also not gone up, CD rates have also not gone up to that extent. So, when do we see that there is a catch up in pricing across the board?

Uday Kotak: Kunal, if you're not getting good pricing on term deposits from any bank, you are most welcome to speak to our bank, we have significantly moved our term deposit rates and we would welcome you and the customer to keep in term deposits with us, in case the policy of your firm allows you to do it.

Kunal Shah: Overall thing is in terms of maybe 60 or 70 odd bps we are also at 6.2 currently and further increase out there but still, maybe I have to look at it.

Uday Kotak: Kunal, you would be in the high network customer base segment where we pay even higher so, and you can see our rates on our website where for high net worth we are paying you 6.6 in case that would interest you a little more and five crore plus if I'm not mistaken at 6.6. So, please look at it and you please look at the rates what we were one year ago and on savings deposits at the last I saw was a one of the banks actually dropped savings deposit rates for amount below 10 crore.

Kunal Shah: Okay. No, so when do we say.

Uday Kotak: I can assure you one point we are not dropping rates.

Kunal Shah: Okay. No, but catch up on the deposit growth that will be required given this kind of momentum on the loan growth side and credit cycle is also there, in terms of demand is also very high. So, finally we have to see it from the system so are we like just few months away wherein we see this kind of rate action across the board?

Uday Kotak: No, term deposits we are very clear we are pricing on market and we obviously look at the marketplace, we look at the benchmarks and which is why if you look at our term deposit growth we are pretty healthy.

Kunal Shah: Sure. And secondly, in terms of.

Dipak Gupta: Kunal there is also a decision between incremental and stock. What will impact your incremental and what will impact your stock, at this point of time it looks comfortable with incremental. So, why are you so keen that everyone increases the price of the stock.

Uday Kotak: Kunal and also it's not about benchmark or anything, but we are all aware about the fact that we as of 30th September sit on a CASA ratio which is 56.1%.

Kunal Shah: And in terms of credit cycle, so when there is such kind of a pass on which is happening in few of the segments being EBLR linked, no doubt we are coming from a very low level, but maybe within a very short span when the raised get passed on, do we see that eventually maybe when the portfolio seasons and a few quarters down the line there it will be credit cost issues in any of the pockets, and that's where you would want to strengthen the underwriting standards as well?

Uday Kotak: Kunal underwriting standards are a constant thing which we evaluate at every stage. And we are very focused on risk adjusted returns. And irrespective of how the finance office or analysts or investors like to look at in, in my view, as a banker for all these years, the concept of operating profit and net profit are inconsistent. In a banking business the credit cost is a core part of an operating profit and anyone who looks at the two separately is making a cardinal error in looking at the banking business in two separate parts because it's one and the same thing, the difference between the two is only the time, therefore you may get a short term boost to operating profit and credit costs hit you with a lag. And I would strongly recommend please look at the two lines together when you're looking at a banking business. It is a core part of a banking business and we look at the credit cost as an integral part of a decision making upfront when we underwrite.

Kunal Shah: Sure. And one last question on distribution and syndication. So, the debt seems to be still not overall within the fee income pie that seems not to be growing and lower than last year's run rate as well. So, is it more to do with syndication or anything on the distribution side as well that there is something….

KVS Manian: So, there is some impact on both, of course you must remember that we had an extraordinary year on DCM last year. So, it is moderated from there downwards and obviously given the flows into the equity side of the business there is also an impact on the distribution side. It's a mix of both.

Moderator: Thank you. The next question is from the line of Seshadri Sen from Alchemy Capital. Please go ahead.

Seshadri Sen: I have two questions. One is on the margins, is a large part of which is coming from the front ended asset re-pricing, what is the expected timeline before which the margins start to normalize, when you look at your book how long do you think this is going to last where margins will be elevated because assets are re-pricing faster than deposits. And what are your plans to mitigate it, loan mix change is one of them that you've been discussing but is that going to take care of that normalization when it happens I presume somewhere like 24?

Uday Kotak: Seshadri you have to keep in mind that there are two counter forces working. Of course, it depends on the situation at each bank with the mix between CASA and the rest of the liability franchise. A lot of the book is getting priced off repo. So, it's your judgment about where you think the repo rate peaks. And that would determine the one side movement on the floating rate book as we go forward, of course it's linked to MCLR which is not linked to repo, but a larger part of the book is linked to repo. So, that is one side of the equation. The second side of the equation is, the rest of the non-CASA deposits, the costs are rising. So, that will be an increased cost on the liability side and then of course how well banks can manage the absolute percentage level of CASA. So, these, the absolute percentage level of CASA out of the total deposits, the cost at which the balance deposits delta cost goes up versus on the asset side, the terminal rate at which repo rate sort of slows down, are the three most important variables in terms of how the pricing and the spreads will go. And of course it's also linked to the mix, the mix of our book. In our case, we have seen a reasonably significantly faster growth in across the board our retail assets. And even the commercial assets compared to the wholesale assets, our mix besides unsecured retail, even in the broader retail assets both consumer and commercial have grown faster, which normally have higher yields compared to the wholesale assets. So, it's a mix change beyond unsecured retail, where again as you know that we are increasing that as a percentage of total mix, our retail and commercial growth on the asset side continues to be robust. And the whole liability side equation I've discussed.

Seshadri Sen: Understood. So, another question is on the more addressed to Dipak is on the tech spend, and it's heartening to see that you are aggressively spending, because banks probably need to catch up a little bit. What are the key metrics that you are tracking in terms of return on that tech spend and how has there been, how have they delivered so far, what are the timelines by which you and as an appropriately you will not disclose all the details, as analysts and investors what is that that we should track to figure out whether these things actually delivering results.

Dipak Gupta: You see, from a tech spend and return point of view, you must look at two separate pieces. One is where you can bring about reasonably direct relatedness between input and output. Which is normally on, let's say the journey part, which is really the engagement pieces. You invest in, do it yourself journeys, you engage a lot more of the customers on your net, and mobile, and you see a direct output really, so that's one piece. The second piece really is more to do with the back end, which is resiliency, scale, where you build capacity and you build sustainability. Now, that results in customer satisfaction over a period of time and hence, to some extent it becomes a non-compromisable irrespective of the cost, it becomes base stakes. So, at this stage, if you see the spend is happening on both sides, A) which gives you direct benefit, and B), which creates a strong foundation which ensures that the customer stays with you or has reasonable reason to stay with you. And for example, if you want your systems up 99.99% of the time really, it's very difficult to say, what did it result in terms of outcomes, you had far more satisfied customers, they stayed with you, they did a lot more transaction that's very difficult to quantify in terms of outcomes. But when you spend on engagement, you have direct outcomes. So, the two are measured differently and we do have metrics or more for the latter than the former peace ready.

Moderator: Thank you. Ladies and gentleman due to time constraint, we take that as the last question. I now hand the conference over to Mr. Uday Kotak for closing comments. Over to you sir.

Uday Kotak: Thank you very much. Wish you all a very Happy Diwali and let's watch the macro and micro as we go forward into the rest of this fiscal year. Thank you very much.

Moderator: Thank you sir. Ladies and gentlemen on behalf of Kotak Mahindra Bank, that concludes this conference. We thank you all for joining us and you may now disconnect your lines.