Emkay
Your success is our success

Punjab National Bank

Conference Call Transcript

Transcription

27 January, 2011

Moderator:

Ladies and gentlemen, good afternoon and welcome to the Q3 FY 2011 post results conference call of Punjab National Bank hosted by Emkay Global Financial Services. We have with us today Mr. K.R. Kamath, Chairman & Managing Director. As a reminder, 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. If you should need assistance during the conference, please signal an operator by pressing * and then 0 on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Anish Damania, Head of Equities at Emkay Global. Thank you and over to you Sir.

Anish Damania:

Hello everybody, thank you for joining us today, wish you a very good afternoon. We would like to welcome Mr. Kamath, CMD Punjab National Bank and thank him for giving us an opportunity to hold this Q3 call. I would now like to hand over the call to Mr. Kamath. Over to you Sir.

K.R. Kamath:

Thank you Anish. I am along with my both ED Mr. M.V. Tanksale and Mr. Rakesh Sethi, my General Manager handling investors Madam Sushma Bali and our AGM handling the finance department. I will quickly run through the presentation. The operating profit for the nine-month period grew by 31.13% whereas the net profit grew by 16.69% over nine month period, now total business crossed the milestone level of 5 lakhs by reaching 5,10,000 Crores recording a growth of 26.15%, total assets grew by 24%, deposits also grew by almost same level at 23.48%, but the credit grew by 29.82%. Coming to the quarter ended reference, the interest income grew by 32.11% to reach a level of 7119 Crores, interest expenses grew by 23.28% and the net interest income has improved by 44.80% by almost 1000 Crores compared to last year at 3203 Crores. The other income was standard basically on account of the treasury operations; I will touch on it a little later. The operating expenses had an increase of almost 469 Crores at 37.74% mainly on account of provisions which we had to make for the second pension option and gratuity. The operating profit for this quarter increased by 29.24% at 2350 Crores, however the provisions grew by 56% from 807 Crores to 1260 Crores which has brought down the growth of net profit to 7.8% 1011 Crores to 1090 Crores. Now if you take the treasury operations out of the net profit and the operating profit you see that our net profit has grown by 16.69% because last year we had a treasury trading profit of 157 Crores and this year it is 87 Crores, of course last year we had 71 Crores from the sale of housing finance company stake. If you take it out I would say that treasury profit and the depreciation have remained at the same level, but the growth in the net profit has been 16.69%, same case with operating profit, if you look at the operating profit without treasury it is 36.17% growth compared to last year. In terms of the provision, we made a provision of 1260 Crores as against 807 Crores last year. The major heads of provision are 555 Crores for NPS and 545 Crores for income tax. Apart from this standard advances provision has increased from 10 Crores to 81 Crores. Now while the income tax does not require any explanation, on the provision of the NPS of course there has been some increase in the NPS, but apart from that one needs to realize that a requirement today to maintain a provision coverage ratio of 70%, so if there is any incremental delinquency though the regulatory provision required is 10%, we need to provide 70% so that we do not slip on the provision coverage ratio. If you look at it our provision coverage ratio is around 78% now, that means any incremental advance you need to cover by 78% to maintain this ratio, though regulatory provision requirement is only 10%, that is why you will see the provisions increasing in the banks. Second, increase in the standard advance provision is more on account of the incremental provision that was to be made on account of the so called teaser loans and the incremental risk weight on some of the big ticket housing loan accounts.

Moving to further break up of income interest income grew by 31%, interest and advances grew by 31%, and interest on investment grew by 27%. The other interest income grew from 28 Crores to 137 Crores mainly on account of 107 Crores one time interest received on the income tax refund. The core non-interest income was 647 Crores. The recovery in return of assets improved from 77 Crores to 123 Crores. The trading profit came down from 157 to 87, I have talked about it. The overall total income for the quarter was almost at 8000 Crores, 7976 Crores which recorded a growth of 27.9%. Now the other free income if you look at it, the processing fee was almost stagnant almost compared to last year 102 Crores. LC/LG commission improved from 133 Crores to 149 Crores a growth of 12%, bills and remittances increased by 17% and one notable increase was in the income from ATM operations which comes to us when our ATMs are used by other bank customers. Last year it was 35 Crores, this year it has been 57 Crores which has been a substantial increase. One fall this year has been last year we called 112 Crores dividend from mutual funds, this time it is only 17 Crores because of the pressure on the liquidity. The exchange profit recorded a good growth from 80 Crores to 125 Crores recording 56% growth.

Now when you move to the interests paid on the expenditure side, interest paid increased by 19.84%, other interest expenses increased because of the interest what we paid on the tier 2 bonds. The interests paid on borrowings have substantially increased this year compared to last year because this year we relied on reverse REPO and CBLO for funding, but last year it was not there, it was more of investing in the liquid mutual funds. Now, establishment expenses have seen a growth of 46.93% basically on account of 360 Crores provision what we made, now 360 Crores I need to clarify that 125 Crores is towards incremental liability on the gratuity, now we have identified this liability at 500 Crores and we have been providing at 125 Crores every quarter, this third quarter we have provided 155 Crores, I think next quarter if you provide a similar amount that liability is taken care once for all. Now, the incremental pension liability on account of second pension has been recognized at 3600 Crores, that means if you amortize it to five years you have to provide something like 720 Crores per annum and we have been providing 125 Crores per quarter, two quarters we provided 250 Crores, so the gap for the current year is 470 Crores out of which 50%, 235 Crores we have provided now, 235 Crores we will provide next quarter.

Now, looking at a futuristic outlook of this numbers, next year onwards we need not provide for 125 Crores towards gratuity, so in the first two quarters we have provided 250 Crores for gratuity and pension, next two quarters we have 360 Crores each, but next year onwards we need to provide 180 Crores per quarter, so this liability I think we are in a position to take in our stride and meet this liability without any additional burden or pressure on the P&L account. Other operating expenses increased by 19%, so overall total expenses were at 5626 Crores. The cost of deposit for this quarter was 5.20, yields and advances were 10.59% and the net interest margin for this quarter was 4.13%. Return on asset was 1.27 for the quarter, return on net worth 22.40, cost to income ratio 42.13% and the book value was 628.9 and earning per share is 138.25. Now you have seen that the NIM has been consistently improving from 3.91 in the first quarter to 4.06% in the second quarter to 4.13 in the third quarter and the overall NIM for nine months has remained at 3.99% as against 3.58% last year. This is in brief my performance for the last quarter but I would like to quickly take you through the number for nine months also. Interest income increased by 23.42% and the interest expenses grew by 9.49%, so the net interest income over the nine months period has increased by 46% from 6003 Crores to 8778 Crores. The other income has recorded a negative growth of -7% because of the treasury impact. The operating expenses have increased by 28.28% and the operating profit has moved from 4994 Crores to 6548 Crores recording a growth of 31.13%. The provisions have been 3316 Crores compared to 2223 of last year, so 49.12% is the increase in the provision mix resulting in to a increase of net profit by 16.69% from 2770 Crores 3233 Crores. Nine months provisions if you look at it, the provision for NPS was 1462 Crores as against 532 Crores last year. Standard advances 159 Crores as against 10 Crores last year. Depreciation and investment 125 Crores as against 75 Crores last year, income tax 1424 and 1552, so overall 3316 compared to 2423 Crores last year.

Now, interest on advances and investments grew almost by 23-24%. Other income grew by 30%; overall interest income growth was 23.42%. Other income, there was a negative growth I talked about it. Core non-interest income grew by 6.75%. The trading profit last year was 666 Crores, this year it has come down to 246 Crores. Recovery and return of assets last year was 176 Crores, this year it is 288 Crores. Of course the break-up of nine months and other things, I think we have put these numbers on the website, I think you can access these numbers now. The cost of deposit for nine month period was 5.09%, cost of fund was 4.44%, yield on advances was 10.48%, yield on investment was 6.58%, yield on fund was 8.06%, the overall NIM over last nine months was 3.99%, so the return on assets was 1.34% for 9%, return on net worth is 22.15%, cost to income ratio is 41.77%. In terms of our business, the total business grew by 26.15%, the deposit grew by 23.48% and the advanced grew by 29.82% and the CD ratio is at 76.59%. The bulk deposits increased from 46,000 Crores last year to 64797 Crores this year, a growth of 40%, the share of bulk deposit has increased from 19.71% last year to 22.43% this year. This is obviously because of the fact that there has been a growth in the credit by 30% whereas the deposits grew by 22-23% and retail deposit growth has been very sluggish in the industry, so you need to make good the deficit by resorting to bulk deposits, but the point to be seen is that are you maintaining net interest margins, we have improved, to that extent there is nothing wrong in going in for these bulk deposits as long as we are in a position to maintain our NIMS. The savings bank grew by 23.73%, the CASA grew by 21.96% and the share of CASA in total deposits is 39.05%.

The credit growth I talked about it, 30% the international growth was 76% and domestic growth was 28%. The food credit growth was 25.9% and the domestic non-food credit growth was 28%. The growth has been well spread. Agriculture grew by 24%, industry grew by 28%, MSME manufacturing grew by 30% and large industry grew by 28%. Retail loans have grown at 22% of which housing is 20%; education loan 25.2% and other retail loans are at 29.2%. The commercial real estate exposure came down year on year, both in absolute and in percentage terms. Our share of the commercial real-estate advances in the loan book is now 4.7% which has gone up to 7%, now it is 4.7% and in absolute terms this is 9729 Crores as against 10551 Crores last year. In terms of the industry sector wise growth again I would say it has been a well spread growth with the food processing recording 12.49% growth, chemical recording 13.89% growth, cement and cement products recording 17%, basic metals recording 15.35 Crores, gems and jewellery recording a 13.23% growth, infrastructure, there is a major growth, power has grown from 22, 567 Crores to 53,787 Crores recording a growth of 49.72% and telecom has also grown by 44.49%. We will try to give you the break up of this maybe later in the evening. I have the numbers here, in terms of power, the liabilities totally 12,516; the overall outstanding is 12,516 Crores, if you try to bifurcate it in to different things power based on coal is 4200 Crores and hydro is 2432 Crores, transmission is 5051 Crores and SEB is another 4500 Crores, so it is again in power I would say that it is well spread, similarly in telecom also if you look at it, the passive infrastructure creation it has gone about

1100 Crores for telecom towers, working capital others for the telecom is 2600 Crores, the overall for the telecom 2G, 3G licenses is about 5500 Crores, again I would say this is well spread numbers here.

Investment book, I think there is nothing great to talk about. 90.85% of the SLR is in STF and 77.55% of the loan book is in STF and SLR constitutes 26.55%. Now NPA, marginal increase in the NPA, incremental delinquency during the year has been 3104 Crores, but cash liquidity has been 955 Crores during this year compared to last year full year 950, this is nine months 950. The upgradation was last year 263 Crores in nine months, it is 232 Crores this year, the write off last year was 483 Crores, this year 590 Crores. After eligible deductions the net NPA come to 1575 Crores now, recovery and return of assets have increased from 176 Crores to 288 Crores this year. The NPA numbers it is 2.03% for the gross, 0.72% for net and NPA coverage is 77.18%. Incomes of capital adequacy, the capital adequacy ratio is 11.90%, this is on account of the RBI requirement of not considering the current year's income in to the capital, if you factor this our capital adequacy ratio works out to 13.31%, our capital adequacy tier 1 at 7.58 now will get improved to 8.99% if you add back the profits in to the overall capital funds of the bank. Market share has improved in deposits from 5.32 last year to 5.56 in credit, 5.43 last year to 5.63 and business per branch has touched the 100 Crores level. There has been no significant change in the shareholding pattern and of course in the international forays we completed the acquisitions of 64% stake in Dena Bank. This is the nutshell of performance for three months and nine months, now I am available to any questions from the investors and analysts. I will hand it back to the moderator.

Moderator:

Thank you, Sir.. The first question is from the line of Suresh Ganapathi from Macquarie. Please go ahead.

Suresh Ganapathi:

Some of the important things. First of all on pension, this 3600 Crores, is that the final actuarial estimate or there is going to be further upward revision?

K.R. Kamath:

See as on date it is final because it is always taken on the basis of the current yields. Now, the current yield is at 8.25%, we have taken this liability at 3600 Crores and this liability is subject to variation depending upon the fluctuation in the yields.

Suresh Ganapathi:

Okay, fine because the earlier was 2500 right, if I am not wrong, so that has gone up to 3600, is it not only because of yield but more number of employees have joined the pension bandwagon, is that a fair and honest assessment, why it has gone up?

K.R. Kamath:

2500 was just a back-of-the-envelope calculation, there was no background to this, we just made an estimate and started providing for it, now that we have the number of employees opting for it and the actuarial valuation available based on the GSEC (ph), so this number is final for the time being.

Suresh Ganapathi:

The next question is on your CASA that has gone down from 200 basis points, I understand that you have taken bulk deposits, but in the environment when interest rates are further going to go up is that a wise move because now you will also have people shifting from saving to term deposits and you had earlier guided that you would like to maintain your CASA at 40% and it already at 39, so just your strategy on that, what is your intention, how do you plan to take it upwards?

K.R. Kamath:

In fact, when I gave my guidance of 40% on CASA I was very clear that CASA in isolation does not convey anything to me, CASA along with net interest margin makes a sense because as long as I am in a position to maintain my net interest margins there is nothing wrong if I go for some bulk deposits and fund my credit growth rather than holding on to 40% CASA and then sacrificing the growth, so if you have seen that the credit is growing at 30% today and the deposit has been growing at something like 22-23% and this 22-23% also includes the bulk, so if you take the retail deposit growth in the industry today, you find that the SB, savings bank is growing at around 23-24%, the current account is growing around 12-13% which has got lot of quarter-end temporary funds available in the system, now if you look at the retail term-deposit both in the industry during the current year, it is very sluggish, it is around at something like 10% or so, now the answer is not very difficult to find because with high inflation if the returns on the deposits or low, definitely the depositors will look for alternative avenues to see that their principal is protected or at least insulated from the inflation effect, so to that extent one need not be very sort of possessive of a CASA number at 40%, while CASA gives you an advantage in terms of the pricing of your loan products also it is not sacrosanct because if there is a demand for credit there is nothing wrong if you look at the bulk, so at 39% we do not infer anything else other than it is a temporary aberration and we stand by our original guidance of keeping it around 40%.

Suresh Ganapathi:

Final question on asset quality. The slippages particularly this quarter is closer to about 10 billion rupees a bit higher than the 9 billion rupees that you reported in the previous quarter, I mean they were something like zoom developers in the previous quarters that went bad, I mean the slippage ratio is still high you know as a percentage of opening advances it is still hovering around 1.9% which is actually higher than the industry standards, so can you just give us an outlook as to where do you see this slippages stabilizing. I understand that, you always have the view that NPL will not necessarily peak, it will grow up, but I just wanted to understand in terms of how do you view the slippages, how do you plan to control, whether there is any large bad account, large account which has gone bad this particular quarter, just some colour on your slippages particularly this quarter?

K.R. Kamath:

I think I again stand by what I said in the last three quarters that I am not a person to say that NPA have peaked at any point in time, I always believe that as long as you lend, as long as there is different trade cycles operating the NPAs will have to come out and NPAs will continue to increase and the two things what I always see is that one is that do you have capacity to handle these NPAs an the second is that do you earn enough to provide for this and my answer for both these questions have been always yes and continues to be yes today also. Now having said that as rightly said there can always be one or two accounts which can totally make a difference in your calculations, so if you look at it today out of this amount I would say that if you take five accounts it constitutes about 600 Crores, we are quite hopeful that these accounts will be upgraded during the next quarter, so it is a temporary aberration, but still I would say that I will again go back to my original guidance saying that as long as my gross NPAs remain around 2% I have no reason to panic.

Suresh Ganapathi:

Just any colour on the sectors which have gone bad on this 600 Crores roughly, is there any common sector basically?

K.R. Kamath:

No.

Suresh Ganapathi:

So it is well spread out throughout the sector.

K.R. Kamath:

Yes.

Moderator:

The next question is from the line of Jatinder Aggarwal from RBS. Please go ahead.

Jatinder Aggarwal:

As you go forward which is rolling 12 months, do you think that these margins are sustainable at these levels?

K.R. Kamath:

Margins will never be sustainable at 4.13% per quarter, now I have been saying this every quarter and improving, so you need to infer something from that. I will say that 4% margin is very difficult to maintain, but we will definitely be better than the others and we will keep our lead in the margins.

Jatinder Aggarwal:

Sir what type of ROA do you think we can come to as we go forward?

K.R. Kamath:

I said 1.3; at the beginning of the year I had given you 1.3, I think I will hold on to 1.3% now and probably after I complete my year end I will have a relook for the next 12 months.

Jatinder Aggarwal:

You would not like to guide for the next 12 months as of now?

K.R. Kamath:

It is better to take stock of the situation at the end because this fourth quarter makes all the difference in a year, so the fourth quarter numbers will be very conclusive in completing this year and probably in one financial year I will try to give a guidance for the next one year.

Jatinder Aggarwal:

So if you aggregate all the slippages that we have seen during the year, slippages in nine months, they have actually overshot what we actually had as additions in the last year itself, so your cumulative book of some of these NPL which are likely to be recovered as you go forward hypothetically should have increased, could you give a broad sense of what is this type of a book?

K.R. Kamath:

Can you repeat the question?

Jatinder Aggarwal:

We have actually had lot of gross NPL additions over the last two years and we have also had a lot of fair amount of write off, could you give a sense of this book size over the last two or three years, how much has been totally written off?

K.R. Kamath:

I may not have the number immediately on the write off book per se, but then one should see that if you look at the write off and you also look at the recovery and return of assets I think you will find a trend that the recovery and return of assets had also substantially increased.

Jatinder Aggarwal:

Which is what I want to understand is that trend on a sequential basis quarter-on-quarter has been raising, so how do you see that line item behaving as you go forward?

K.R. Kamath:

I think I expect the recovery in return of assets to be quite contributing to my system at least because if you have written off something in the last two years definitely it has to add to my recoveries in the next one year, so obviously I will think it would be much better than last year.

Jatinder Aggarwal:

Does this year actually form a base in terms of operating performance and next year should be better because your operating cost my sense is that they seem to be stabilizing given the fact that we have actually charged off gratuity this year.

K.R. Kamath:

That part is taken care of by incremental provision requirement on account of gratuity provision and everything now comes down to 180 Crores per quarter from next year as against 250 Crores which has been provided in the first half and the 360 Crores which I am providing for the next two quarters this year. That is I think taken care, but the operating expenses can go because we plan opening up some 200-300 branches next year and then of course the income from that will flow after this, so always there is a cycle but we would say that we would like to work on something like 40% cost to income ratio, maybe temporarily it can go up to 41 and go to 42 and come back to 40 sort of a situation, but the broad guidance on the cost income ratio will be around 40%.

Jatinder Aggarwal:

And credit cost should not materially increase compared to what we have seen in the first nine months?

K.R. Kamath:

Again, I have a divergent view on this credit cost concept itself because credit cost when you talk you should talk on the regulatory provision that is required vis-à-vis the credit but today if you are maintaining a 78% provision coverage ratio, and you provide more money for maintaining that 78% and then you factor it as a cost of credit I am totally in a disadvantageous position compared to a bank which is not providing for the credit for the delinquencies.

Moderator:

The next question is from the line of Hiren Dassani from Goldman Sachs Asset Management. Please go ahead.

Hiren Dassani:

Sir couple of questions I see your commercial real estate exposure has declined on a year-on-year basis and also from March to December. Are you looking at further curtailing it down?

K.R. Kamath:

I will not use the word curtailing it down, we have been moderate.

Hiren Dassani:

Any sense on what is your exposure to let us say aviation and microfinance industry?

K.R. Kamath:

Microfinance is about 1000 Crores; aviation 4200 Crores.

Hiren Dassani:

There are also some concerns about some of the new telecom operators, I mean the new 2G operators, and so do we have anything substantial there?

K.R. Kamath:

I do not think one should give a knee-jerk reaction on that. On the 2G licenses, I made this clear, my liability to overall liability under 2G is about 550 Crores in the form of a bank guarantee, now out of this, this 210 Crores is bank guarantee in limit which the party was enjoying and whatever is above 210 Crores that is 340 Crores is fully covered by deposits, now this 210 Crores is also covered by 10% margin, that is 21 Crores, so if you take this out my net exposure other than deposit to 2G license is 189 Crores, now that is nothing you know and I do not think that the government will get in to a situation where they cancel these licenses and send a very wrong signal to the international market, so the whole thing we expect is that, there can be some penalty or something levied and then ultimately the caravan will move on.

Hiren Dassani:

Just to understand this of the total 13,500 Crores exposure to telecom, you are saying that the exposure to the new 2G license is only 550 Crores and of that also other than 210 Crores everything is secured by cash, at this point in time you have 20 Crores of guarantee.

K.R. Kamath:

Correct, so 189 is the net exposure on this 2G thing.

Hiren Dassani:

Sir, one keeps hearing that after this whole episode of the CBI arresting some officials the whole process of sanctioning has kind of slowed down and it has become much more, I mean people are becoming much more risk averse while sanctioning fresh loans, any comments you may offer?

K.R. Kamath:

I would say that people will be a little more cautious now, not risk averse, it is desirable in the interest of the industry that you are a little more cautious than what you are in the past.

Hiren Dassani:

Okay, but as bank have we changed any processes or any structure in terms of credit approval?

K.R. Kamath:

No, we had a well laid out credit process and whatever some officer is involved from our side as per the media we gather and other things the loan is closed in our books, there is nothing wrong in the note, now if behind the scenes somebody has paid some money to somebody I do not think that one should worry about the credit process or the credit quality.

Moderator:

The next question is from the line of Amit Premchandani from UTI. Please go ahead.

Amit Premchandani:

Just a question on the overall macro with short-term rates at around 9-9.5% when do you see the end demand getting impacted if the short-term rates continue to be at these rates?

K.R. Kamath:

My own view on this is that the next quarter is also going to be a little tough in terms of liquidity and in terms of interest rates, now the issue is that when the inflation is almost at 18 and if you compensate the depositors at very low rates whatever deposit growth we are seeing may evaporate from the system, so today instead of worrying on the credit growth one need to worry on the deposit mobilization and there is a need for us to increase the rates of interest in deposits in such a way that keeping deposits with the bank does not become counter productive to the depositors. Having said that if you increase the rate of interest on deposits, you have to necessarily pass it on to the borrowers and a question comes up to what level you will be in a position to pass off, now from our side I would add in from picking up a question from the last time that was there any response from the bank on the things happening in and around us, there were short-term loans which were getting disbursed from the banking industry which was a product which is an innovation out of short-term liquidity available. Today we have stopped this type of short-term loans which are on unsecure basis and which are just given because you get a PDC and then somebody whom you feel is a good credit risk is taking it a reasonably good return, so today we are looking more in to the purpose, ensuring end use and also the returns on this, so to that extent I would say that the credit growth which was coming from the short-term loans sort of situation will taper off whereas the genuine credit demand will continue and we feel that the normalcy if you look at the industry growth credit growth is always peaked at around 20% for the system and I do not think that this 20% will be an issue anytime even for the industry system I am saying.

Amit Premchandani:

And on the overall deposit rates as you mentioned that deposits interest rates have to go up, they are just 1% below the peak level in 2008, till what time do you expect this deposit cost to go up and reach that peak level and how does it affect the overall margin, I know your margins are relatively much higher than the sector, but for the overall system as such?

K.R. Kamath:

See, deposit cost going up it has always got a lag impact, now in an increasing interest rate scenario if you increase the rate of interest on both sides, it is time to benefit because your loans get reprised immediately and your deposits get repaid over a period of time and you have seen this because we have been increasing the interest rates on both sides now and you have also seen an increase in our NIMS because of this lag effect, interest rates falling down, the effect will be the reverse on the NIMS, now if you look at it I feel that last quarter, suppose this quarter there is no interest rate increase, then you may find a little pressure on the NIMS because the full blown effect of the interest on deposits will come in to picture and the full-blown effect of the interest on advances have already come in to picture last quarter.

Amit Premchandani:

Right Sir, and in terms of the percentage of assets which are linked to PLR and linked to base rate, can you give us a broad picture for PNB?

K.R. Kamath:

I do not have the right numbers on hand, but if I can give you a ballpoint number it is around 35% on the base rate and around 35% on the BPLR and the remaining is not linked because it is our regulated risk like agriculture, loans against deposits, all these things.

Moderator:

The next question is from the line of Amit Ganatra from Religare. Please go ahead.

Amit Ganatra:

What is the total balance sheet size?

K.R. Kamath:

3,43, 000 Crores.

Amit Ganatra:

You mentioned that there is some interest on income tax refund?

K.R. Kamath:

107 Crores of interest on income tax which came which has been factored as income from other sources during the current quarter.

Amit Ganatra:

Is it forming part of your total interest income?

K.R. Kamath:

Yes, 107 Crores.

Moderator:

The next question is from the line of Manish Chowdhary from Citi Group. Please go ahead.

Manish Chowdhary:

I just wanted to check on your growth likely, currently it is running at about 30% on the loan side, what do you think is a sustainable number for you both for this year and for the next year possibly?

K.R. Kamath:

25% should be a very quite achievable number because last year fourth quarter saw a good growth, so the base impact will be felt this time and I think we should end up the year with 25% growth in credit and we have normally been growing 2% above the systems growth, so the system is projected to grow at 20%, we will keep ourselves a goal of 22%, but something between 22-25% should be a doable number next year also.

Moderator:

The next question is from the line of Nandita Parker from Karma Capital. Please go ahead.

Nandita Parker:

I was puzzled by your answer about deposit rates going up, since you recently had increases in deposit rates have you not seen an increase in mobilization in the last couple of weeks?

K.R. Kamath:

I think it is a race between interest rate and inflation rate, so by the time I increase the interest rate, the inflation went beyond that.

Nandita Parker:

But you have seen an increase in deposit mobilization?

K.R. Kamath:

Not as much as I wanted it to be, you see the retail deposit growing at 10-11% I am not happy with that, I have been growing at 17, 18, 20% on deposits, suddenly if this number comes down to 11% I am not happy on the retail side I am saying.

Nandita Parker:

Secondly the bankers have been asking the RBI for improved liquidity as in CRR cuts, what is your sense of that?

K.R. Kamath:

The bankers have nothing to lose in asking you know. They will always ask to improve liquidity and increase the rate of interest both does not go together, so it is for the RBI to balance this. There is a need for increasing liquidity but there is an inflation which is at 10% today and the food inflation is at 18%, so the RBI has to do a balancing act and I think the signal coming from RBI is that if it is to handle only one that is inflation first.

Moderator:

The next question is from the line of Manish Karwa from Kotak. Please go ahead.

Manish Karwa:

I just wanted to check how do you calculate your base rate and what factors will drive the base rates going forward? I understand that we have to review this base rate at least once a quarter but if I just look at your reported funding cost or cost of funds or cost of deposits, they have not gone up much but I believe incremental deposit cost would have gone up quite a lot, so I just wanted to understand which is the biggest factor that is driving the base rate calculation?

K.R. Kamath:

I think we have shifted the base last quarter to the incremental deposit rate.

Manish Karwa:

So if that is the way then obviously incremental deposit cost would have gone up further up in January and whenever you review a base rate I believe that could further go up?

K.R. Kamath:

Yes, that has to be seen in the backdrop of the RBI policy announcements also and then probably one will look at these numbers.

Manish Karwa:

When you say incremental will it be a fair assumption to make it will be about a one-year deposit cost?

K.R. Kamath:

Yes.

Manish Karwa:

Does having a 40% CASA have any influence on that? You having a 40% CASA would that also be a factor of your base rate calculation?

K.R. Kamath:

My colleagues are telling me that we are looking at the current quarter's cost, so the current quarter's deposit cost has increased, so to that extent there is an upward bias on that. When you take the current quarters deposit it also factors the CASA.

Manish Karwa:

Okay coming in this quarter the March quarter then as interest rates are going up and if the incremental CASA proportion might be lower then your incremental deposit cost can rise much faster which could lead to a faster rise in base rate?

K.R. Kamath:

See, the point is that if you are not getting the retail term deposits and if you are relying on the bulk deposits for funding your credit growth the incremental cost is going to go up and then the interest rates have to be pushed up.

Manish Karwa:

Lastly of your total loans how much would be on PLR and how much would be on base rates now?

K.R. Kamath:

I just answered this question 35% roughly, 35% on both sides and the remaining 30% is not linked to both.

Moderator:

The next question is from the line of Mitul Patel from Laburnum Capital. Please go ahead.

Mitul Patel:

Hi, just wanted to ask regarding the pension expense, has it been finalized that you guys are going to amortize in the next five years and not three years?

K.R. Kamath:

We are still awaiting the final guidelines from the RBI but we understand that it is likely to come to amortize over 5 years.

Mitul Patel:

But would not things change if IFRS kicks in, in the next two to three years with your pension accounting sort of deferred when you get that stage?

K.R. Kamath:

See if IFRS kicks in what will happen is that it is coming from 2013 April that means we will three years 2011, 2012, and 2013 and then 2014, so even if you have to kick in to the IFRS in 2013, you still get 4 years time to provide for it, so it is a question of factoring the difference between 5 years and 4 years in the fourth year.

Mitul Patel:

Sir, this gratuity is going to be 180 Crores next year going forward for quarter and this is going to be an ongoing thing because it would not make a difference if you add more employees in the future, you are adding more branches, it would not increase from 180 Crores?

K.R. Kamath:

New employees are going to the defined contribution scheme and this will not put a liability on the defined benefit is ours now, so it is based on whatever returns we get on the pension fund, we give them the pension, so there will not be any incremental liability on account of new employees in the banking industry.

Mitul Patel:

One last question is that the 250 Crores per quarter will end in next quarter?

K.R. Kamath:

Not 250 Crores, it will be 360 Crores for next quarter and thereafter it will be 180 Crores per quarter.

Moderator:

The next question is from the line of Amandeep Goraya from Finquest Securities. Please go ahead.

Amandeep Goraya:

Sir just wanted to know like in third quarter there has been a restructuring of 817 Crores rupees account, so from which sector or which segment this has come?

K.R. Kamath:

I think I have given the updated list of the restructured book in my website which gives me an update of everything, 817 bifurcation I may not have immediately.

Amandeep Goraya:

Sir, till now out of the cumulative restructured accounts almost approximately 9% of them have slipped to NPA, so any guidelines like what are the expectation of any percentage on like if you can give in to slipping in to NPAs?

K.R. Kamath:

We have been talking on the subject, I think we had said that somewhere around 10% should be a number and hardest that is like the rating agencies who were talking about 16-17% at the beginning, they came down to 15%, then we said that this is the time to make a truce between 10 and 15%.

Moderator:

The next question is from the line of Ajinkya Dhavale from Bajaj Alliance Life Insurance. Please go ahead.

Ajinkya Dhavale:

Sir couple of questions on other income. The core fees are not growing this quarter that is question number one, so how do you paint the picture in the future, if I see the growth of the core fee income it is just in single digits.

K.R. Kamath:

Overall it is in single digit, but if you get in to further bifurcation I find that the LC, LG income that is the income coming out of letters of credit and bank guarantee, that has grown at 12.40%, the income coming from bills and remittances have grown at 17.3%, income from ATM operations have grown up 60.76%, so the only hit which came in the other income, the major hit, last year I got dividend from mutual funds, that is liquid mutual fund to the tune of 112 Crores which is a product of excess liquidity, this year it is only 17 Crores, so I lost 100 Crores of income from the liquid mutual fund compared to last year, it is one area where I lost and the processing fee, it was 5 Crores less than last year, so I think in this quarter I should be in a position to make it up.

Ajinkya Dhavale:

Sir loan growth is so strong now we would expect that fee income moves somewhere close to that even if I adjust that mutual fund income still the fee income growth is not in line with the balance sheet growth or is there some pricing issues?

K.R. Kamath:

To some extent I would say when you are trying to sanction bulk loans like in the power sector and other things there you cannot proportionately charge the processing fee in terms of percentage will come down when you are handling the larger thing and then we went with a festival bonanza for about four-and-a-half months on the housing loans where we waived this processing fee and other things to attract the retail and if you have seen the retail has grown almost by 20% which was never done by the bank in the past, housing loan grew by about 20% which was never there, it was about 12, 13% last year, so temporarily we sacrificed this processing fee but if you look at the 9 months period you find that processing fee has increased by about 10% over last year, our LC, LG commission has increased by about 23.57% and other income of course in terms of percentage looks very high because of the smaller base, so basic if you look at nine month income, dividend income from mutual funds came down from 275 Crores to 96 Crores, so this is a major reason for other income effect, otherwise I would say that it is nothing to worry.

Ajinkya Dhavale:

But is it fair to assume a 20% plus growth as sustainable in to the next year?

K.R. Kamath:

We are working for that.

Ajinkya Dhavale:

Second thing there is a lot of variation in the income from foreign exchange if I see quarter-on-quarter, is there the propositions adverse impact, in the second quarter it was 31 Crores and third quarter 125 Crores, last year third quarter it was 75, so it does not seem to be an annuity income anywhere, can you please explain that?

K.R. Kamath:

It depends on the type of foreign exchange volumes what you handle but if you look at over a nine-year period, it has seen a growth from 200 Crores to 270 Crores, something like 35%.

Moderator:

Thank you. The next question is from the line of Shrey Loonker from Reliance Mutual Fund. Please go ahead.

Shrey Loonker:

Sir just if you could give us some sense what has been the composition of the incremental loans that you have given out over the last two to three months more in terms of short term, long term working capital, nonworking capital. If you could give us some colour on that?

K.R. Kamath:

I mentioned about it a lot in the last quarter substantially we reduced the short terms loans, which are given in the form of unsecured short term loans, which were rising out of the excess liquidity in the system but then I think if you look at the format of the loans more in the form of term loan because even the people for working capital requirement today would like to convert their working capital demands of loans and limits in to WCDL that is working capital demand loans to take advantage of the interest arbitrage but otherwise it will be a term loan both for the capital expenses and for working capital demand loans for the working capital purposes.

Shrey Loonker:

Sir, if you could just explain what is the interest arbitrage between converting of WC into WCDL?

K.R. Kamath:

See, what happens is that normally when you sanction a credit limit you would have put some rate as per the rating BR plus, if the base rate for 3%, 4%, but when it comes to the short term loan people give it for three months it depends up on a three months money market, three months market rates. So today if you look at some of it somewhere this three months rate can be some thing like base rate, which is 9%, whereas the party may have some 11-12% on its CC rate and in such cases of party shopper out and anyhow they do not gives your CC limit. So in a way it helps me to increase my outstanding credit and increase my interest income. In a way it does not impact me adversely, but it impacts me positively by that. If the party is already using its CC limit fully, we do not encourage him to take these working capital demand loans.

Shrey Loonker:

Sir secondly if you could just give us a sense how the pricing power is today with the bank. Obviously it seems a little higher because you see margins expanding?

K.R. Kamath:

I think, you ask me banks I do not know if you ask me PNB yes it should be.

Shrey Loonker:

Sir if you could just given the sense for up to what level do you think you can be in a much more a dictating situation and after which you know after what point of time you think the borrowers will start seeing the bench and passing excessively?

K.R. Kamath:

It is not that the borrowers come here and surrender that you charge me more. The borrowers are negotiating. It is only the question is that I am in the position to hold on to my differential interest rate compared to my peers. So it is only a question what you hold compared to others if somebody is charging 8, I cannot sit here and charge him 12. So what I do is that if somebody is charging 8, I would like to try charge 8.5 and that where you feel that there is the net interest margin difference between me and others.

Shrey Loonker:

Let me put it this way, if there is another 100-bips rise in the base rate are in the cost of funding of PNB over the left to the next twelve months. How may do you think it will be able to pass it on to your borrowers?

K.R. Kamath:

What will happen is it is a vicious circle. The moment I increase my interest rate on that borrowing and if there is a resistance in absorbing that interest rate then the interest of the credit goes through slowdown. When the credit goes slows down I have no need to mobilize deposit aggressively. So I lower by the deposit rates so whole game is to protect the NIM. It may not be at 4.13%. I definitely make a point of it cannot be 4.13% but it is to be some thing better than the PF. That is what I would say.

Shrey Loonker:

Sir if you can just we have been aggressive on the bulk market and which is a fair point you made that as long as you are making money on the bulk money there is no harm in being in it. But just wanted to get a sense on this incremental bulk deposits also would the lending out of that incremental bulk deposits also will be maintaining NIMS of 3% plus?

K.R. Kamath:

That is how my NIM has started increasing. If you look at every transaction to see that you maintain your NIMS.

Shrey Loonker:

The last question sir, if you could just give us some more granular sense in the commercial real estate and how you see it and how do you think your portfolio is behaving and if you could just give us some further sub-split into the commercial real estate segment?

K.R. Kamath:

We do not have an anxiety on commercial real estate as of now. Our exposure to commercial real estate has come down both in terms of absolute and percentage terms. We are a little cautious on funding this segment because obviously the effect that side which is coming out of very close scrutiny by the regulators also. So we are selective we do not say that we do not lend. The customers who are with us for ages they get support a good rent discounting sort of a proposal will get support may be hospitality industry will get support but just giving loans for may be construction of malls or construction of the housing complexes left and right sort of decision may not happen. So we will take a cautious view but nevertheless we are not totally averse to fund the segment.

Shrey Loonker:

If you could just give us some further broad sub-spilt into the commercial real estate how much will be to real estate developers and how much will be decentered hovering around the hospitality?

K.R. Kamath:

I have no numbers immediately available with me on this count, but by just my memory to source me properly, we had about 3000 Crores of a loan given to the real estate rent discounting. The remaining part was either for development of housing properties are may be for some and that it also includes somewhere if we are given I think this is what is the break-up. I do not have the numbers ready with me.

Shrey Loonker:

Sure no problem sir, very helpful thanks you very much.

Moderator:

Thank you. The next question is from the Utkarsh Maheshwari from Reliance General Insurance. Please go ahead.

Utkarsh Maheshwari:

Sir I just had a look on your restructured book it is close to 14,000 Crores as of now, right?

K.R. Kamath:

Yes.

Utkarsh Maheshwari:

Sir can you guide us I mean which are the primary sector which are actually slipping into that what we call as NPA category from this particular sectoral break-up because I think we have shown some 1255 Crores of restructured assets slipping into NPA. I mean any ideas the sector, which are actually coming in from?

K.R. Kamath:

I may not have this 1250 solid break up out of this, but I can only tell you that there is a concentration in the results.

Utkarsh Maheshwari:

Sir you have mentioned in the opening remarks regarding the gratuity provision. I think that is 500 Crores ad hoc right and this is the only thing I mean for this quarter which has not been made?

K.R. Kamath:

Yes the 125 Crores if I cover for one more quarter that liability is that.

Utkarsh Maheshwari:

Yes, I mean only the pension is the recurring one.

K.R. Kamath:

Yes that is 180 Crores for quarter.

Utkarsh Maheshwari:

Yes thanks a lot sir. I am done.

Moderator:

Thank you. Ladies and gentlemen that was the last question. I would now like to hand the conference over to Mr. Anish Damania for closing comments.

Anish Damania:

On behalf of Emkay I would once again like to thank all of you for joining the call. Thank you very much Kamath Sir and your team for the call and have a great evening.

K.R. Kamath:

Anish you should tell everybody that we are coming to Mumbai for an analyst meet on Monday that every question get exhausted today. Alright see you on Monday.

Moderator:

Thank you. Ladies and gentlemen on behalf of Emkay Global financial Services that concludes this conference.

Note: 1.This document has been edited to improve readability.

2. Blanks in this transcript represent inaudible or incomprehensible words.

Emkay Global Financial Services Ltd.
Paragon Center, H -13 -16, 1st Floor, Pandurang Budhkar Marg, Worli, Mumbai – 400 013. Tel No. 6612 1212. Fax: 6624 2410