“Karnataka Bank Limited

Q1 FY 24 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to Q1 FY 2024 Earnings Conference Call hosted by Karnataka Bank. As a reminder, all participant lines will be in the listen-only mode, and you will be able to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing star and then zero on your touchtone phone. Please note that this conference is being recorded. I now hand over the conference to MD and CEO Mr. Srikrishnan H. from Karnataka Bank. Thank you, and over to you, sir.

Srikrishnan: Thank you very much.

Good afternoon, ladies and gentlemen. I am Srikrishnan, the MD and CEO of Karnataka Bank. I am here on behalf of the Board of Directors, and I want to thank you for participating today. Joining me are Sekhar Rao, our Executive Director, and senior management team members: Balachandra, our Chief Operating Officer; Abhishek Bagchi, our CFO; Gokuldas Pai, our Chief Business Officer; and Sham K, our Company Secretary.

Today is historic day for us due to the new management's inauguration. Just to clarify, I have been with the bank for slightly under two months, and our new Executive Director has been on board for around four to five months. As we move forward, expect to hear more from Karnataka Bank under the tagline: "Banking with a legacy and embracing the future". Today, we are discussing the bank's future based on our recent quarterly results.

We recently informed the stock exchanges about our highest-ever quarterly net profit: INR 370.70 crores, compared to INR 114 crores from the same period last year. Three critical metrics define our bank's performance: growth in advances, growth in the book, and deposit growth. Our advances have seen a year-to-date annualised growth of about 10%, and for this quarter, we achieved 5.4%. Our deposits increased by nearly 8%, with a healthy CASA mix maintained at around 32% - 33%. Historically, our CD ratio reached its peak at 70%.

Our net NPA decreased significantly to 1.43%, down from the previous year. We've worked hard on recovery and controlling slippages, which currently stand at 0.5%, compared to 3.31% last year. Even compared to the last quarter, there is a reduction of about 27 bps. We also proudly announce our provisioning at a record high of 83.47%. The good news is also about the core provisions which stands at about 62% as against 55%. Additionally, we've maintained our NIM guidance within the 3.5% to 3.71% range.

Regarding our bank's growth, our Return on Equity (ROE) is an impressive 17.7%, with a Return on Assets (ROA) of 1.47%. Our cost-to-income ratio is competitive within our banking segment at approximately 47%. Lastly, despite asset growth, our CRAR is at a solid 17%, with Tier 2 steadily maintained.

With its rich tradition and exceptional customer service, Karnataka Bank operates 900 -odd branches throughout the nation, over 60% of which are in Karnataka. We're present in 14 economic zones, and our goal is to evolve from a regional story to a national story. Our strategy is three-pronged: efficiently run the bank, grow the bank by adopting a more outward-looking approach, and change the bank by embracing innovation.

We sort them all out, make them all more efficient, lot of centralization of processes and making sure that, the optimal efficiencies that we derive, not only on the cost, but also the turnaround time as far as the customer journey is concerned. Now the capacity is in two parts, one is related to the operational side, the other is related to technology. Both is something that you know we are definitely augmenting here as you know the new management. The second part is that along with that we need to grow the bank. Now when I talk about grow the bank, we need to change the culture of the bank. The culture of the bank has been not so outward looking and there is not much of a sales culture which is including deployment of sales teams outside of the branches.

So far, they have been only looking at the channels of sales which is the branch channel. We are, introducing essentially the sale channel both on the asset side as well as on the liability side for CASA as well. And these are teams that will be deployed in branch serving areas in and around the branch to get the new to bank acquisitions. So, the NTB numbers, which is currently at about 4,000 odd accounts per day is going to move up and that's the second piece of growth. The other part related to grow the bank is also to make sure that in addition to the DSA channel, there is a huge amount of digitization that, we have already invested into.

And we are just on the verge of launching many such journeys, whereby the digital channels of the bank, which include the mobile as well as our browser-based internet banking channels, will be translated, just not but transformational, but also everything to do with transactional. So, which means that we would actually be in a position to acquire clients end to end. Most of the digital journey is almost 100%. Some of the journey is near 100%, whereby all of the new customer acquisitions need not necessarily have to be physical.

And that's a new channel that we are building. In addition to the existing channels, which is the branch channel, which we are activating fully, and this also now would be helped by the sales channel, which is the DSAs, as well as the sales teams, the feet on street, who are deployed on the ground. And the last one, which I talked about, is the digital. So, this is essentially the grow the bank culture that we are bringing in. And here, there's a lot of reorientation that we need with all our existing workforce and most of them are receptive.

The last about you know 40 days that I have been going around the regions, visiting them etc., I have a fair pulse of the bank of the ground level you know impressions as well. And the third piece is changing the bank. Now this is a transformational journey in the overall scene. What we are trying to do is that organically while I was talking about the growing part related to the three channels of client acquisitions, new customers, etc., there is also an existing customer base of 1.3 crores that we have. And we need to make sure that there is a lot of upsell and cross-sell that is possible for this huge customer segment.

To transform and evolve, we've established digital and analytical centres of excellence housed in a new 40,000-square-foot office in Bangalore. This not only facilitates the digital journey but also positions us in India's Silicon Valley. And here, talent acquisition is also possible currently, the very reason being that we are sitting in the heart of the Silicon Valley of India, that is Bangalore. Now given this, change that we have, instrumented over the last about 30 to 40 days. We believe that, this digital journey that we are undertaking will be far easier because the investment not only in technology, but investment into processes and we have also taken some help from external consultants here, whereby the analytics related to our existing customers on their behaviour, on what products they use, based on their transactions, what other products they could potentially use is being extracted.

Those cuts are being given to the branches and to the sales channels for them to actually go and acquire new customers. Along with that, the existing customers for new products. So, this is the upsell, whereby the share of the wallet is going to pretty much increase. Now this is step number one, as far as the change the bank is concerned. Step number two is all about innovations and collaborations.

Now the bank will innovate but obviously we are not a FinTech, so we are not like some of the technology companies which are innovating and creating breakthroughs and really looking at some kind of a new product which is like, completely digitized but they cannot scale up. So, we have already launched this program called KBL-FinOne, which essentially is a FinTech collaboration whereby we have identified three or four product areas, which include some of the asset side, which is related to co-lending, as well as, consumer loans, and also a lot on the MSME side. Now, these are the FinTechs or some of the new age companies who are focused on certain segments, and they will collaborate with the bank, and we will scale that up whereby we acquire clients, we also give them a wider range of services including other banking services which we can offer. But on the other side, the FinTech benefits a lot because scaling up is something that the bank is ready to do.

We want to work on the inherent strengths of this bank. The inherent strength of this bank lies one in Karnataka, as a geography, but we want to expand to other regions also.So, whatever we do well in Karnataka, we want to make sure that we do it even better in the other states where we have the presence. And it is not a small presence because most of the states that even typically take Maharashtra or even take some of the other South Indian states, we have an excess of fifty branches in each of these states. Now what we are trying to do is to make sure that the geographical strength that we have acquired in Karnataka is something that we will replicate.

Our bank's strengths lie in sectors like MSME lending and agri-lending. In addition to providing financial services to these sectors, we also facilitate government payments, soon to encompass direct and indirect taxes.

So, we are in the process of creating online as well as portal-based, which is a complete revamp of our website and also allow all of these third parties to come in and make sure that we are working with a very open but very systematic and information security control portal. The last part is that we are very big in agri-lending. As a percentage of our total loans, agri forms a major part.

Now agri-lending, retail and MSME opportunity is there in these segments. Now we believe that we can help a lot in the agri also. The reason being that here again, there are a lot of value addition that we can provide because the fact that, access in terms of telecom access and connectivity has already been provided by a lot of service providers in the country. So thereby, we are able to actually get going with just adding more products to it and delivering them digitally.

So, this is the other piece which is related to change the bank. So, in terms of the overall summary, ladies and gentlemen, what we are trying to do is to run the bank more efficiently and simplify a lot of processes, grow the bank organically and change the bank to introduce a lot of inorganic but not acquisition based but collaboratively from other third-party players. The bank in addition offers a complete you know suite of personal loan products that includes insurance, investment as well as broking and these are again done through the third-party initiatives that we have already put in place.

So, the bank can help in protecting our customers for both life as well as non-life and health. And likewise, we can also help them to facilitate the trading in case, they are interested and so on. So, this is basically a quick summary of, what and where we are and what we want to do. The results are very encouraging.

The results are very encouraging, the reason being that the bank on a financial positioning is also well placed. From the overall management team, yes, there could be potentially a lot of lateral hiring that we need to focus that we have talked about in the existing plans. We will supplement them with a lot of specialists depends on whatever kind of specialists are required where we cannot fill up the gap from internal resources. But we do have a very good management team already. And we believe that, we are really creating a digital bank of the future.

Now on that note, I think I have done my introductory talk. And I'll hand it over back to the moderator for the next steps here. Now, Sekhar, is there anything else you want to add?

Sekhar Rao: Perfect. I think so you've covered it all. I will just add a couple of comments in the closing remarks. This is a pretty good summary of where we are headed and where we are.

Srikrishnan: Thank you. So, moderator back to you, please.

Moderator: Thank you very much, sir. We will now begin the question-and-answer session. We'll take the first question from the line of Sushil Choksey from Indus Equity Advisors. Please go ahead.

Sushil Choksey: Congratulations on a great set of numbers, and best wishes for all the aspirations which you just highlighted. Question number one, so you had given a broad vision in one of your media interactions when you commenced, what a journey to get to INR1 lakh crores, which means 18%, 20% growth year-on-year. Can you highlight a bit on that?

Srikrishnan: Thank you for your insights, Mr. Sushil. Our annualised growth rate currently stands at approximately 10% for our advances book, while our liability side is nearing 8%. Our goal is to double these figures within the next 3 to 3.5 years. This implies an 18% to 20% compounded quarter-on-quarter growth annually. To put it simply, within the span of 3 to 3.5 years, our figures should more than double their current state.

Our initial target was to surpass INR 100,000 crores in our total asset book within that timeframe. Reflecting on our performance after the June results, without making any forward-looking statements, I can confirm that we've already crossed the INR 150,000 crores milestone in our overall business growth, and we're just entering August. This significant growth from our previously declared figures showcases the effective changes implemented in our frontend branch channel.

In the upcoming quarter, we will introduce our second sales channel, followed by our third channel focusing on digital acquisition. With these steps in place, we are confident in our trajectory and believe robust growth is achievable for both our assets and liabilities.

We need to meticulously monitor our metrics, particularly those that are crucial for success. This includes ensuring our net NPAs and gross NPAs stay within controlled parameters, as well as maintaining stability in the NIMs. We're currently facing challenges in managing costs, particularly with the rising cost of deposits. However, despite global increases, such as the Federal Reserve's rate hikes, we believe that deposit rates in India have reached their zenith.

Given this scenario, we're optimistic about maintaining our current NIM ranges. We plan to achieve this by strategically adjusting our asset growth and ensuring optimal pricing. I trust this provides clarity on our approach moving forward, Mr. Sushil, and addresses your query.

Sushil Choksey: So where do you see your cost of deposit of 5.1 currently to by the year-end and cost of funds which is at 5.2 by the year-end?

Srikrishnan: Our cost of funds has historically ranged between 4.7% and 5.5%. We aim to maintain this range, although it's influenced by seasonal variations. To illustrate, consider the patterns of our clients, including contractors and agricultural farmers.

Farmers, for instance, tend to withdraw significantly from their Current Account and Savings Account (CASA) during the sowing period. However, post-harvesting, we've observed a consistent trend: our CASA witnesses an influx as farmers deposit their earnings from crop sales back into the bank. This cyclic nature highlights the bank's established CASA retention strength. Similarly, contractors often see delays in payments, be it from government projects or other contracts. These delays can sometimes lead to temporary CASA withdrawals. Yet, over time, they revert to maintaining substantial deposits with us, which indicates trust and a stable banking relationship.

Furthermore, we've yet to fully launch our government business operations. Once initiated, the government business's float is expected to decrease our overall cost of funds by a few basis points initially. As we further expand this segment, we anticipate additional opportunities to ensure our cost of funds remains within the targeted range.

Sushil Choksey: My next question is, your vision is more about co- lending, growing retail, and the bank was ready on technology, but I think the current management team brings a lot of bandwidth with the vision to empower the digital technology transformation to a next level and the next support which will be required for that is human resource. So how are we planning our TAT, which was brilliant in the first half of last year, I don't know the reason we slackened a bit, but all these measures are going to bring in a fantastic change as it's visualised in the stock price too. So, what kind of spending are we going to do annually for this year or next year to enable all these growth paths and the vision which you are carrying today?

Srikrishnan: That's a noteworthy observation, Mr. Choksey. Over the years, we have invested heavily in technology, maintaining a core solution with Finacle that's been operational for over 23 years, complemented by several auxiliary systems. Investments geared towards digitisation focus on streamlining customer onboarding journeys and enhancing data analytics to optimise our cross-selling capabilities through various channels.

While these investments are in place, the products deriving from them haven't been launched. Our immediate strategy pivots around product development and launching, but equally crucial is integrating contemporary technology and business process methodologies. This is why I emphasised our intentions to conduct significant lateral hiring.

However, despite these developments and the bank's current cost-to-income ratio standing at 47% (considering provisions for certain statutory actuarial valuations related to superannuation and contingencies like the bipartite settlement), we project an initial ratio of around 48 to 50%. This is expected to decrease as revenue scales, aligning with our forward-looking investments.

In essence, while we do seek specialists, both the executive director and I are confident in our ability to attract top-tier talent. Our institution's legacy, combined with the promising trajectory we offer, makes a compelling narrative for potential hires looking for substantial career growth."

Moderator: We will take the next question from the line of Sarvesh Gupta from Maximal Capital. Please go ahead.

Sarvesh Gupta: Good afternoon, sir, and congratulations on a good set of numbers. Sir, what would be your guidance for the growth rate in terms of both credit and deposit, as well as CASA? Where would you want to reach by the end of or the exit quarter of this financial year?

Srikrishnan: Good afternoon, Mr. Sarvesh. Thank you for your question. Based on our current trajectory, our annual growth rate for advances is approximately 10%, which places our current total advances at around INR 63,000 crores. Therefore, by the end of the financial year, we anticipate that this figure could likely reach between INR 73,000 crores and INR 75,000 crores.

Regarding our CASA, our CD ratio presently hovers between 68% and 70%. Our ambition is to elevate this ratio. This implies that our assets will see faster growth than our liabilities, though we're confident that liabilities won't fall far behind. Specifically, for liabilities, we project growth of about 10% to 12%, positioning us to achieve a target close to INR 1 lakh crores.

Given these projections, the bank's turnover should appear much healthier by year-end, potentially surpassing the INR 1,75,000 crores mark. To put it into perspective, we currently stand at INR 1,50,000 crores. I hope this provides a clearer picture of our anticipated book size, Mr. Sarvesh."

Sarvesh Gupta: Understood. And one problem which I think most of the small and mid-sized banks have been facing is the trouble in gathering enough CASA. So, I mean, you did talk about making it more sales-oriented and all, but I mean, if you can throw some more light on your path towards sort of doing a better job on the gathering of CASA, this has been sort of ailing, most of the banks in your, at your size and scale? And secondly, you talked about a lot of transformation-related hiring as well as technology, so will that affect materially any of your cost-to-income ratio in this financial year, or you feel that you have enough cushion or the investments have already been done?

Srikrishnan: As I mentioned earlier in response to a previous question, we are actively seeking new talent. However, we're specifically targeting specialists who possess skills and expertise not currently present within our existing team. That is our primary approach.

In terms of cost-to-income ratios, there might be short-term fluctuations. While our current ratio stands at 47%, it could momentarily rise to 49% or even 50%. However, we anticipate this to decrease in subsequent quarters for two main reasons. Firstly, our capital concerns will be addressed. Secondly, as our revenue grows, it will naturally counterbalance the cost, leading to a more favourable ratio.

Regarding the Net Interest Margin (NIM), we remain committed to maintaining its strength. Reflecting on past performance, there might have been areas where we could've been more effective, just as some of our peers in the mid-size segment faced similar challenges. However, at present, our direction is guided by a clear and focused strategy."

Sarvesh Gupta: So, on the CASA side, what's the sort of aspiration in the next one years, two years, three years, where can we reach?

Srikrishnan: As I mentioned earlier, our goal for the next three-and-a-half years is to achieve a certain target,. However, if we break this down using simple mathematics and aim to bring our CD ratio closer to the 80s from its current position of around 70, it implies that our CASA and overall funding must sufficiently support that number. This includes the hundred thousand figures plus any additional calculations you might infer. This target sets our broader vision, but it's crucial to implement it step by step. This is where the new management's focus lies. As of now, we're actively on our execution path, and the entire team is fully behind this initiative.

Sarvesh Gupta: Thank you, sir, and all the best.

Srikrishnan: Thank you so much.

Moderator: Thank you. We'll take the next question from the line of Suraj Das from B&K Securities. Please go ahead.

Suraj Das: Yes, hello sir. Thanks for the opportunity, and congratulations on your appointment. Couple of questions, you laid out the reason for the next couple of years. So, sir, I was asking, you laid the foundation or reason for, what you are going to do in the next couple of years in terms of growing the bank or a couple of changes that you have highlighted. I just wanted to know, let us say, slightly from a longer-term next three years to five years, what kind of, let us say, products or segments will be in your focus. So, in terms of loan mix, what kind of loan mix, we'll see. Let us say, by 2026 or 2027, when you build that one lakh crore of asset side book? So that would be my question number one.

Srikrishnan: Mr. Suraj, as is often said in sports, we must approach each game, each session, one step at a time. Drawing parallels from cricket, there are distinct strategies for different formats, and forecasting a three-to-five-year game plan requires us to deeply consider our current execution. While I'm more comfortable discussing a three-year outlook as I've mentioned in previous responses the real challenge lies in our strategic approach.

We're currently emphasising three primary sectors: MSME, agriculture, and retail. Our growth strategy is three-pronged: utilising physical branch channels, sales channels, and digital channels along with collaborations. This strategy shifts our reliance from a single engine of growth to three potent engines. In time, I anticipate each engine will perform with equal vigour, distributing business more evenly. Central to our future growth is the development and optimisation of these engines. That's our current focus and direction, Mr. Suraj."

Suraj Das: Okay. So, the currently the share of retail if I see in your presentation, there is something like 50%, 51%. So, over the next couple of years, is it fair to assume that this share would increase to something like 60%, 65% or so?

Srikrishnan: On the topic of advances, retail currently stands at roughly 50-51%. We're witnessing significant growth in areas like gold loans and home loans, among others. However, while these sectors expand, we're also shifting our focus towards MSMEs and mid-sized corporates – areas the bank previously didn't prioritise as much. This segment is bound to grow as well. Therefore, it's not just about retail's percentage increase; it's a comprehensive growth across all three key segments: MSMEs, retail, and agriculture. As for specific percentages and how they will evolve, let's give it a few quarters to see the emerging trends, after which we can more accurately adjust and align our objectives.

Suraj Das: Okay, understood, sir. The second question is, sir, on the underwriting side, have you done any changes or let us say, you see any gap, where you can fill in or any kind of action you have taken just wanted to know. You have said many things about many changes on the product side, on the sales side, on the marketing side. However, on the underwriting asset quality side, have you done any changes, or you are taking any action there?

Srikrishnan: I appreciate your question. One unique strength of this bank is that even at the branch level, both branch managers and their assistants, regardless of whether the branch is in a rural or semi-urban area, are adept at writing credit proposals and overseeing credit evaluation and monitoring.

Another key asset is our team of over a hundred agricultural field officers dispersed across the bank. I'm working to centralise their efforts in the field. Many peer banks face challenges in assembling such a qualified team skilled in agriculture – our officers are both academically trained and honed their skills within the bank, making them well-equipped to navigate agri loans and the agri business supply chain.

To enhance our efficiency, we're taking several steps. Firstly, we're expanding our underwriting capability by increasing our regional processing centers from five to eight, ensuring faster loan approval processes. Secondly, we're making significant investments in technology, emphasizing workflow and document management processes to promote efficient and paperless information transfer. Lastly, as part of our efforts in digital loan origination, we're in the process of developing credit scoring models that facilitate quick, digital approvals using precise parameters. By analysing available data, we aim to refine our scoring models and increasingly base them on observed behaviour. This holistic approach is what we're implementing to elevate our services.

Suraj Das: Okay. Thanks for the detailed answer. And the last question from my side, sir, in terms of your return ratio, ROA and ROE, whatever kind of vision that you are having and the kind of transformational journey you are on. So, upon completion of this journey, let us say next two years to three years, what kind of ROA, ROE on a steady state basis, the bank can generate? Have you given any thought on that, or have you made any projection to that, that the kind of business model that you are developing, what kind of ROA, ROE on a steady state basis, you want the bank to deliver?

Srikrishnan: So Mr. Suresh, the ROE, ROA is a derivative of how well we do on the other parameters. So, what happens there is that, if you do all of this right, then the outcome of that will be the ROE and the ROA. Currently what we are doing is that we do have a current healthy, ROE of almost like 17% plus, right? Now that is a very good kind of a sign. The other is that, the ROE currently is at 1.47%, but we would definitely be hovering in the same region of about 1.2% to 1.4%, and that is a stated objective again. So, this would bring in a lot more value to the stakeholder on a long-term basis and that is something that, we are quite confident about.

Moderator: We'll take the next question from the line of Chintan Shah from ICICI Securities. Please go ahead.

Srikrishnan: Good afternoon, Chintan.

Chintan Shah: Good afternoon, sir. Thank you for the opportunity. Sir, just two- three data keeping questions from my end. Sir, firstly, if you could just provide the breakup of GNPA movement into slippages, write-off recovery and update for the quarter?

Chintan Shah: Yes. Okay. And secondly, sir, also, could you just provide the breakup of loan book into fixed and floating and how much would be linked to a repo rate and MCLR? And lastly, sir, on the CASA breakup, if we could just have help us with the number of current CASA means CA and SA? And lastly, as on the income part, other income breakup...

Srikrishnan: The first part related to the gross and the net NPA and the additions and reduction. That's what you wanted, right?

Chintan Shah: Yes.

Srikrishnan: In terms of our overall gross NPA, the additions for this quarter amount to INR292 crores. Up-gradations stand at around INR90 crores while recoveries are at about INR167 crores. Technical write-offs are relatively small, coming in at about INR10 crores, which includes other write-offs. The total for this quarter is INR269 crores. I mentioned the gross NPA as a percentage earlier, which has shown healthy performance compared to both the previous quarter of last year and the preceding quarter of this year. That indicates the direction we are taking. Your next question pertaining to the EBLR rates and their percentage in relation to the overall gross credit. Approximately 20.31% is on the MCLR, while EBLR linked rates are around 6.54%. T-bill rates account for about 46.94%. This gives a comprehensive view of the percentage distribution for the gross credit. Lastly, you had a query regarding CASA. Could you please restate that question?

Srikrishnan: Allow me a moment to check the numbers. Our savings accounts hold approximately INR 23,077 crores, while the current accounts have around INR 4,658 crores. Additionally, there's a minor float, estimated to be slightly less than INR 250 crores to INR 260 crores, spread across overdraft (OD) accounts and other floats.

Chintan Shah: Sir, this is very helpful. And sir, just lastly, on the other income part that are INR324 crores. So in other income, could you help us with the breakup at least in the treasury and on non- treasury and or fee income.

Srikrishnan: For the quarter, the total trading income has been only about INR8 crores. And the depreciation on investment has been about INR43 crores. And the other, which is...

Sekhar Rao: INR273 crores.

Srikrishnan: The fees and commissions amount to INR273 crores. This includes third-party fees, ATM charges, and all other commissions. To provide a more detailed breakdown: the total encompasses service charges, guarantee commissions, insurance commissions, ATM interchange fees, locker rental, among other things. If you need a detailed breakdown, we can provide that information to you offline.

Chintan Shah: Sure, sir. I will take that offline if required. Thank you so much for patiently answering all the questions, sir.

Srikrishnan: Thank you so much.

Moderator: Thank you. The next question is from the line of Anand Dama from Emkay Global. Please go ahead.

Anand Dama: Thank you, sir and congratulations for your appointment. So first, in your presentation, you talked about retail share. I think that is a RAM share, right? Because retail, as such, it is very misleading. So that is number one, if you can change that in your presentation going forward. Sir, second is that, if you look at Karnataka Bank we have been tracking it for a long, long time. Is that the asset quality and particularly the MSME book always has been an issue in the bank whenever basically there are bad asset quality cycles, how do you try and contain this? you said that basically, I mean, bank has a branch led credit processing system right now.

So, first you would want to change that, you would want to change the underwriting the way basically it has been happening in the past across the legacy businesses that they have. And secondly is that, what are the new business lines that you would actually look at? Because bank is already into mortgages, they are doing gold loans, any other new product that you would want to introduce going forward? So, these are the key questions that I have?

Srikrishnan: We're focused on refining our existing products and underwriting processes rather than making drastic changes. The bank has worked diligently to manage slippages, NPAs, coverage, and recoveries. Recognising the strengths of some bank segments, our objective now is to activate newer sectors. We're leaning on past experiences and harnessing digital data. For instance, by observing customer behavior, such as payments for rent or utilities, we can gauge their purchasing power. This insight allows us to offer pre-approved consumer loans based on their activity this is a direction we're keen on exploring. Furthermore, we value the loyalty of our longstanding customers and aim to provide them with more flexibility on the liability side. For those who maintain considerable balances in savings and current accounts, we're introducing a 'Flexi CASA' option, enabling customers to manage their funds via online platforms. We're also expanding our offerings, integrating with customs, GST, and CBDT, to provide versatile use cases directly to the customer, eliminating the need for in-branch visits. One area we haven't previously discussed is our intent to establish a government business vertical. Given our significant presence in Karnataka and existing relationships with various institutions including religious bodies, educational establishments, and more we believe there's an opportunity to serve government departments as well. This initiative represents another facet of our ongoing efforts to redefine our products, redevelop them, and target new verticals.

Anand Dama: But sir, you talked about again the new initiatives that you take, but how do you fix the past?

Srikrishnan : The past is a growing, particularly the cross-sale aspect mentioned earlier. We possess analytics related to each of our existing customers. As a result, we aim to offer additional products with a high level of focus based on their behavior and transaction history. This approach extends to our existing customer base. This is where the analytics factory comes into play, continuously generating vast amounts of data and supplying it to our branches. This data helps guide the branches in suggesting suitable products for certain customer segments, even if the connection is not direct but rather on a larger scale. The power of data enables us to accomplish this feat.

Anand Dama: So, basically if you look at your specific PCR, obviously your NPA is still higher than as compared to some of the other peer banks. But if you look at a specific PCR is still some where's in the mid-60s as such, if you take out the technical write-offs. So, any plans basically to improve that in the near term, consuming the profits that you're actually generating at this point of time, which is very high. So, you run down your book first, and then basically look at taking it past 70% and try and contain the credit cost that will actually flow in the future. So, any thoughts over there?

Srikrishnan: Yes, if we prioritise Non-Performing Assets (NPA) and focus solely on managing them, it might lead to a loss of growth opportunities. Our approach is to strike a balance by emphasising both growth and NPA containment. We have set objectives to reduce NPA rates compared to the previous year and last quarter, and we are successfully achieving this. The trend for both gross and net NPAs is positive.

Regarding the Provision Coverage Ratio (PCR) and net of technical write-offs, you are correct. Our coverage stands at around 62% for these items. However, if we consider even the gross NPA secured by assets like land and buildings, the coverage is approximately 76.5%. So, the bank is well protected, and although certain processes may take time, we are secure.

Our primary focus remains on growth and expanding the book size. As the book size increases, the percentage of NPA may not decrease, but we will address it strategically on an account-by-account basis. It is essential not to confuse the old bank's functions with the new bank's focus. The old bank will continue its existing operations efficiently, while the new bank will concentrate on growth without neglecting NPA management. We are committed to maintaining a dual approach and not giving up on either front.

Moderator: Thank you. We'll take the next question from the line of Ketan Athavale from Robo Capital. Please go ahead.

Ketan Athavale: Thank you for the opportunity. I just wanted to know what is the expected credit cost for FY’24 - 25 in percentage terms?

Srikrishnan: Currently, the credit cost stands at approximately 0.28%. Looking ahead, we believe there is a high likelihood of maintaining this level or potentially even reducing it further. By the end of the year, we anticipate that the credit cost will remain stable and be around the same level, Ketan.

Ketan Athavale: Same for FY 25 also?

Srikrishnan: No, we anticipate a slight reduction, around 25 basis points, in the credit cost. The reason behind this reduction lies in our strategy to focus on digital acquisition. By creating a loan book that primarily comprises salary loans, flexi loans, and other related products, combined with partnerships with payroll processing companies, we can ensure repayment guarantee as the next payroll will automatically come through the bank. This approach will have a positive impact on reducing the credit cost. However, achieving this reduction will require dedicated focus on both the digital side and the development of these specific products.

Ketan Athavale: Okay. Thank you. That's it from my side.

Srikrishnan: Thank you so much.

Moderator: Thank you. The next question is from the line of Manish Dhariwal from Fiducia Capital Advisors Private Limited. Please go ahead. As the current participant is not answering, we'll move on to the next question, which is from the line of Aalok from MNCL. Please go ahead.

Aalok: Thanks for the opportunity and sir, congratulations on a great set of numbers. The presentation which is being put out clearly outlines the vision which the management is looking forward, so this is really commendable. Sir, I had two questions to understand from you? One is more on the asset quality what is that we are looking in terms of the slippages run rate maybe in FY’24 as a whole, including any element of restructuring portfolio that might come out in the coming periods. So that's my first question?

Srikrishnan: Let me address that directly, Aalok. Currently, our slippage stands at approximately 0.5%. Looking ahead, compared to the previous quarter, we have witnessed a substantial reduction, and compared to the previous year, the reduction has been even more significant. This performance represents our best slippage figures thus far. Our goal is to maintain this positive trend and, at the very least, sustain the same level of performance for the remainder of the year.

By achieving this, we can look forward to a healthy outlook by the end of the year. Additionally, as we progress through two more quarters, some other stress in the portfolio will have gone through its lifecycle, further strengthening our position. As a management team, maintaining this level of performance would make us content and confident about the bank's overall performance.

Aalok: So, would you like to give some numbers on GNPA and NPA at end of FY’24?

Srikrishnan: The market standard for mid-sized banks like ours regarding net NPA is to aim for a reduction of around 20 to 30 basis points. We aspire to bring our current net NPA of approximately 1.43% down to about 1.20% by the end of the financial year. Given our relatively low book size, achieving this target requires minimising absolute recoveries and new additions.

Regarding the Provision Coverage Ratio (PCR), we are in a good position with sufficient coverage. This gives us the ability to negotiate and handle any potential slippages, including the possibility of taking haircuts and resolving them adequately. Overall, we have gradually moved towards a reasonable position concerning NPAs. Although not entirely comfortable, we are making progress.

Barring any unforeseen surprises, if the credit monitoring department continues to perform as it has been, and we maintain our focus on NPA management, we should reach a comfortable range of around 1.20% for net NPA. In the next financial year, we will continue working to further reduce it to a lower level. Some of the most successful banks in the country have achieved a net NPA of 1% or even lower, and we aim to move in that direction as well.

Aalok: And sir, would you like to leave us with some number on SMA2 portfolio, how is that looking like?

Srikrishnan: I think I'll ask my colleague Balachandra to answer that question, SMA2.Just give us a minute please.

Y V. Balachandra: As of the 30th of June, the Special Mention Accounts-2 (SMA2) stands at approximately INR 1,197 or you can consider it as 1,200. There has been a slight increase compared to previous periods, attributed to specific reasons. Some sectors have encountered realisation issues due to ongoing political dispensation in particular states.

Aalok: Thank you, Balachandra sir. Sir, a question to you. So, would it be safe to say that now all of the efforts are to realise more toward growth and not at asset quality, also because if I look at the way ALM is positioned, there are drivers for margin expansion from year onward as well, we are at LDR of 70%. So, that gives you a cushion, maybe more on the lending side versus borrowing side and opex while that might see some increase, with the kind of thought process on lending side, I believe it's going to circle more around growth. So how are you looking at that number inching up?

Srikrishnan: Yes, on a blended basis, the monitoring of our operations is carried out between me and Sekhar, who serves as the Executive Director (ED) here. At the vertical head level, there is a strong focus on growth. This focus includes managing both liabilities and assets, ensuring a balance between growth and maintaining quality.

Credit quality is vital for the asset side, but we also emphasise maintaining quality on the liability side. We are cautious about increasing transactions without deriving the corresponding benefit in terms of balances. We aim to avoid the bank becoming a conduit for unproductive volume. Our management team has been guided to prioritise quality on both sides.

To ensure this quality is maintained, we are implementing governance mechanisms and monitoring systems. At a high-level, we are committed to insisting on good quality assets and fostering productive CASA (Current Account Savings Account) relationships. We aim to avoid customers who solely deposit cash without contributing to the bank's overall growth. Instead, we will focus on migrating such customers to digital channels, and we have plans for migration projects to facilitate this process.

Moderator: Thank you. Mr. Alok, we request you to kindly rejoin the queue. Thank you. The next question is from the line of Manish Dhariwal from Fiducia Capital Advisors Private Limited. Please go ahead.

Manish Dhariwal: Thank you so much for this opportunity and my apologies for previously unable to connect. I think there was a problem at my side on the voice track. So, at the outset, congratulations and compliments to the new team, especially the new CEO, Mr. Srikrishnan. So, we wish you all the best as our fortunes are also pretty much, kind of moved with how margin performs. So, my question basically is related to this pay book.

You know, it's a pay book that is across the older banks where they already have a huge chunk of customers who have been banking with them for the last so many years. But then to these customers, these new products are being offered in the line of say, personal loans or variety of other products like car loans, whatever. My question is that these customers typically, are they new to these products or they have experienced these products much from some other originator?

Srikrishnan: Good afternoon, Manish. Based on my personal interactions with customers during branch visits over the last 40 days, I have visited about four to five regions, covering approximately eight branches in each region. This amounts to nearly 40 to 45 branches out of our total network. I have also engaged in discussions with a few invited customers.

A key finding from these interactions is that customers are highly satisfied with the personal relationships they have developed with their branch managers and staff. They express strong loyalty towards the bank and have no intentions of moving elsewhere. However, some customers have sought out new digital products and services that they couldn't find within Karnataka Bank, leading them to use offerings from other institutions.

These customers are digitally savvy and are keen on accessing digital products from Karnataka Bank. Many have personally asked me to bring new products to the bank, expressing their willingness to use them if made available. This presents a promising opportunity for the bank. While the bank's potential has not been fully utilised in the past, I am determined to work alongside the new management team to capitalise on this opportunity. There is nothing like offering more products to an existing set of loyal customers, and we intend to make the most of this situation.

Manish Dhariwal: Absolutely, absolutely. Really, that has to be the first catchment area. I realised that and which is why I was trying to understand whether these were like new to these products, or you were saying that you were kind of...

Srikrishnan: Absolutely, the customers in Karnataka are well-informed and highly aware of the technological advancements and opportunities in the digital landscape. The advent of technology platforms has made them very digitally savvy. They are well-versed with digital solutions and eager to embrace new technological offerings. The market in Karnataka is ripe with opportunities for catering to their digital needs, and we recognise the importance of leveraging their digital awareness and enthusiasm to provide them with the best possible banking experience.

Manish Dhariwal: Wonderful. So now what is, now see, like a very nice and a focused plan has been shared, you in fact shared that with us as well. Now what would be your thoughts on the equity dilution? Because if you're going to be growing fast, then maybe there'll be requirement of fresh capital.

Srikrishnan: Certainly, I understand your interest, but I must refrain from addressing forward-looking statements. However, as an expert in this field, you are aware that banks require capital to facilitate growth. Currently, we stand at a capital adequacy level of 17% overall, and we have a Tier 2 structure in place.

If necessary, we may consider churning the Tier 2 or making changes when opportunities arise. This is a continuous process for banks like ours.

While we aspire for growth capital to support our growth path, I cannot provide specific details about our fundraising plans at this stage. As I have only been in this position for two months, we are still assessing the overall situation. If there were an urgent need for capital, we would have addressed it immediately. However, at present, we believe that we are in a comfortable position. Rest assured, any decisions regarding fundraising will be made with careful consideration and in the best interest of the bank.

Manish Dhariwal: Yes, I think that's what I was trying to understand. Yes, that there is no plan in the immediate term. At a personal level, what do you think are the personal milestones that you are setting for yourself when you've taken up this very interesting opportunity of helping a 100% old bank, but then you know, infusing it with new ideas, new technology, new way of doing things, really waking up a very old organisation. So, how are you taking your personal milestones?

Srikrishnan: Thank you for asking me this, Manish. It's indeed an intriguing opportunity for me. Having worked with several startup-like organisations in my previous roles, including three new banks, joining Karnataka Bank on its 100th year is a particularly interesting challenge. On this momentous occasion, I declared that this bank will be treated like a startup bank. Our efforts are now focused on creating and aligning everything around this narrative.

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

Jai Mundhra: Hi, good evening sir. I wanted to understand a bit on the verticalisation in the non-corporate products. So, retail, MSME, Agri, to what level these products have been verticalised and I think you had said that the branch managers or the select branch managers, they also have a good understanding of the underwriting practices. So, I also wanted to check that, some of the banks of your size, they have a business and risk responsibility lying with the same individual. Is this the same process here, or the business and risk are entirely separate functions?

Srikrishnan: Thanks for asking, Jai. This is about leveraging the bank's strengths in the right direction. We've made progress in verticalisation, appointing MSME National Head, Agri National Head, and separate teams for retail, branch banking, asset, and credit marketing. This ensures clear segregation between retail credit, mid-size corporate credit, and MSME credit.

At both regional and head office levels, there's a structured approach with slab-wise credit sanctions. We have five regional processing hubs, expanding to eight, ensuring smooth flow from branches to regions and the national head office. Turnaround times vary based on the type of credit, faster for retail and a little slower for larger credits. We are committed to continuous process improvements as we move forward.

Moderator: Thank you, sir. The next question is from the line of Saket Kapoor from Kapoor Company. Please go ahead.

Saket Kapoor: Yes, sir. Sir, I missed your initial commentary. So, pardon me for repeating. For exit of FY ‘24, what should be our net NPA level? And NPA as a provision of books, what percentage are we eyeing, sir?

Srikrishnan: Sure, Saket. As mentioned earlier, our exit target for net NPA is around 1.2%, a notable improvement from the current 1.4%. Achieving this target relies heavily on robust monitoring practices. We aim to avoid any unexpected surprises, and at this stage, we have reviewed all regions and accounts, leading us to believe that we are on the right track to achieve our goal.

Saket Kapoor: And provision books, sir? As a percentage, the total loan book, what should be the provision book percentage?

Srikrishnan: The PCR is 83%, as I told you. And for the core book, it is about 62% right now, core provisions.

Saket Kapoor: Okay, sir. And for the NIMs trajectory, sir, I think you were explaining that the cost of funds will go up going ahead. So, taking that into factoring that, what should be our NIM trajectory for the exit of the financial year and also going ahead? What's the…

Srikrishnan: The team has previously mentioned a target of 3.5% to 3.7% for our overall Net Interest Margin (NIM), and we are maintaining that stance. While there is pressure on the cost of deposits, we have some loans and new acquisitions on the loan book that are helping offset this pressure. Despite the challenges, we are committed to adhering to the guidance of achieving a NIM between 3.5% to 3.7%.

Moderator: Thank you, sir. The next question is from the line of Yaswanth Kumar Thippeswamy, a retail investor. Please go ahead.

Srikrishnan: Good afternoon Mr. Yaswanth.

Yaswanth Kumar: Yes, good afternoon, Srikrishnan. And congratulations on the results. And I had a couple of questions with respect to asset quality and the growth. I think you have already addressed that, so I will not repeat that question. So, yes, the question that I have now is with respect to the yield and advances. So last quarter, I remember Mr. Sekhar had identified advances which were yielding less than the government securities. So, I mean, having said this, there was some retiring of advances. So, similarly, I would want your inputs. Have you noticed anything of that sort? And at the same time, can we expect that lead-in advances to improve from here on?

Srikrishnan: Sure, Sekhar is available to address the question. From my perspective, as I joined the bank, one of the first exercises was to review the percentage yield on the asset book based on different tenors. We conducted a thorough analysis and took necessary actions to exit some assets and improve the rate on others, focusing on repricing and continuous improvements.

If you need specific details related to what Sekhar mentioned earlier and how it has improved, Sekhar can provide more insights as he is here with us. So, over to you, Sekhar, to address the last part of the question and elaborate on the improvements made.

Sekhar Rao: Hi again, good to connect with you. These tactical decisions are part of our regular practices. We recently identified an arbitrage opportunity where the advances were yielding less than what was available through investment options. In response, we made the strategic decision to retire those low-yielding advances. Our focus remains on continuously monitoring opportunities to rationalise costs and exit unprofitable buckets and tenors. This process is ongoing and helps us optimise our operations.

As a result of these efforts, our corporate loan book yield has shown significant improvement. It has increased from mid-7% to slightly above 8%, specifically at 8.29%. This reflects our commitment to maximising yield and making well-informed decisions to enhance the bank's overall performance.

Moderator: Thank you, sir. We'll take the next question from the line of Rakesh Kumar from B&K Securities. Please go ahead.

Rakesh Kumar: Yes, Hi, sir. Thanks a lot. So, I have a couple of questions. So, we have a couple of low hanging fruits currently in terms of the LDR number LCR number and we are in a scenario when the credit quality may remain fine for some time. And so, you have that much time, so you have that much time to ramp-up your business in that time.

The question is that we would like to first take a proof of some opportunities that we have in terms of asset mix, LDR number being low, LCR number being very high. Is that the first thing that we are going to do or what is the plan that we have on the branch expansion side, which are the vertical hills that we are going to build-up, which are the loan segments where we are going to increase the market share? So, these three things if you can highlight and the first question also.

Srikrishnan: Absolutely, you are right. We recognise the existing strengths of the bank and have no intention of moving away from them. Instead, we aim to leverage these strengths to their fullest potential.

As part of our strategic goals, we have provided clear targets to all branches and regions to increase the CD (Credit-Deposit) ratio. Initially, the CD ratio stood at around 60% when the new management, including myself and Sekhar, took charge. Through continuous efforts and process improvements, we have seen progress, and the CD ratio has now reached 70%. However, we are not content with 70% and aim to push it further as an immediate target.

Regarding branch expansion, this financial year, we have plans to open around 50 new branches. Additionally, our focus on digital expansion has no boundaries. Significant investments have been made in backend systems and frontend access. Currently, we are working on enhancing product journeys to ensure a seamless digital experience for customers.

We have achieved a digital approval rate of 100% in certain loan approvals, and for others, it stands at around 70% to 80%. Our goal is to minimise manual interventions and repairs, streamlining the process and reducing the cost of acquisition. The investments in technology open up new possibilities beyond just our branch presence, and we are determined to maximise the benefits from these digital advancements.

Moderator: Thank you, sir. The next question is from the line of Saket Kapoor from Kapoor Company. Please go ahead.

Srikrishnan: Yes, Mr. Kapoor.

Saket Kapoor: Yes, sir. The point I was asking earlier on the ROA trajectory also, what the trajectory should be? And for the detection of NPA, how are we using technology, especially AI and the system processes, wherein we will have early detection of NPAs going ahead? And what portion of the loan book is attributed to a personal loan? And that too on the unsecured part.

Srikrishnan: Sure, let me address your questions. Regarding ROA, it currently stands at approximately 1.47, and this figure may vary as we continue to grow our business. While we aim to work towards achieving our targets, we also understand that ROA is subject to change due to business growth. However, we will strive to maintain the ROA within a certain range without divulging specific figures.

As for the investment in technology, we have implemented an advanced system called VasoolSOFt for NPA monitoring and automation. This application ensures that all NPAs are automatically declared from the system. Vasool SOFt monitors and delivers early warning signals (EWS) and even sends out automated notices in case of delays or potential issues.

This automation is not only essential for our operations but also a requirement from the Reserve Bank to minimise manual errors and ensure accuracy. We continuously enhance this system to integrate various processes, including legal and recovery actions, making it a seamless interface across multiple systems.

I hope I have addressed all your queries. If you have any further questions, please feel free to ask.

Moderator: Thank you, sir. Ladies and gentlemen, we'll take that as the last question for today. I would now like to hand the conference over to MD sir, Mr. Srikrishnan H and ED sir, Mr. Sekhar Rao for closing comments. Over to you, sir.

Srikrishnan: So, thank you so much for your participation, from my side as a first time that I have met with the analyst. We have uploaded our investor presentation on our website. This is again, very clearly articulating all of whatever is required and as Sekhar is here and he's been in the bank even earlier than me by a couple of months. I'll hand over to Sekhar for him to do the concluding remarks of today's conference.

Sekhar Rao: Good evening, everyone. Thank you for the overwhelming response. We currently have around 285 participants, and I sincerely appreciate all of you for taking the time to be here. As Srikrishnan mentioned, this is an exciting time for the bank, with record profits and a clear vision for the future. We are a bank with a rich legacy, enthusiastic about embracing the opportunities the future holds.

We have identified specific segments and businesses, namely MSME, Agri, and retail, which we will leverage for growth. Additionally, our extensive presence in various geographies will support our growth in liabilities. Ensuring asset quality remains a top priority, we have established dedicated teams and structures, separating retail, wholesale, asset quality, and credit underwriting functions, adopting best practices for optimal performance.

We are well-positioned for growth and remain committed to keeping you informed about our progress. Srikrishnan and I have taken it upon ourselves to maintain regular communication with all of you. We look forward to having ongoing conversations. Thank you once again, and a special thanks to the moderator for hosting this event.

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

Srikrishnan: Thank you, moderator, for handling this as well. Thank you so much for participants.

Moderator: Thank you very much, sir. Have a great day.