



“Karnataka Bank Q2 FY2019 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to the Karnataka Bank Q2 FY2019 Earnings Conference Call hosted by Centrum Broking Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing “*” then “0” on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Gaurav Jani. Thank you and over to you Sir!

Gaurav Jani: Thank you Raymond. On behalf of Centrum Broking, we welcome you to the Q2 FY2019 Earnings Conference Call of Karnataka Bank. From the Bank, we have with us the MD and CEO, Mr. M.S. Mahabaleshwara, the CFO, Mr. Y.V. Balachandra, and the senior management team. I would like to hand over the call to MD Sir to discuss the results and the strategy forward. Thank you and over to Sir!

M.S. Mahabaleshwara: Thank you Gaurav. Good evening and welcome to you all for this earnings concall of Karnataka Bank for the Q2 i.e. Quarter Ended September 2018. As you all know, banking sector is passing through some tough time even though there is a ray of hope of revival especially in the deposit and advances side. The slow growth phase is still continuing; however, in the banking sector, apart from the growth related issues, the asset quality pressure as well as the provision pressure is also likely to continue during the current financial year coupled with the latest development in the debt market and NBFC sector, the new addition to the woes of banking sector.

With this background, I would like to highlight the performance of Karnataka Bank during the Q2 of FY2019. The interesting thing is that there has been appreciable increase in profits, decrease in NPA, decrease in stress in pipeline, good business traction as well as improved staff efficiency. These are the five highlights of the performance of the Bank.

As far as the profit is concerned, you all know that we have been able to register a growth rate of 19.79% that means, the profit has increased from Rs.93.38 Crores to Rs.111.86 Crores. In fact, the Interest Income has shown 10.22% growth during this particular quarter and NII also has registered 6.24% growth and for the full six months, it stands at 8.29%.

The Other Income, even though trading profit has significantly decreased because during the last quarter of September 2017 we had a trading profit of Rs.85.99 Crores whereas, the current quarter it is just Rs.6.93 Crores, but there was a significant increase in the fee based income, which increased from Rs.161.83 Crores to Rs.194.27 Crores with a growth rate of 20.05%. So with this, we have been continuing our steady growth fee based income also and as such the total income even though there is significant reduction in the trading profit, the total income has shown an increase of 5.62%.

Our efforts to contain the expenditure are continuing and in fact there is a reduction of expenditure to an extent of 2.87% during the current quarter as well. Hence the operating profit, which was Rs.366.24 Crores during September 2017, now it is at Rs.356.33 Crores, so if you look into the trading profit, I think the operating profit even though percentagewise it has come down, in the core sector there is a significant improvement and resultantly the NIM, which was at 3.09% as of September 2017 and 3% as of June 2018, now it is at 2.91%, but for the first six months it is at 2.95%, and therefore, I am very optimistic that by the end of this fiscal, it will be at around above 3%.

As far as the NPA portfolio is concerned, the NPA which was at 4.92% as of March 2018, is easing out and it was at 4.72% as of June 2018, and now it has come down to 4.66%. This is the percentage wise. However, amount wise during March 2018, it was at Rs.2376 Crores, now at Rs.2372 Crores and net NPA, which was at 2.96% during the March 2018 and was at 2.92% during June 2018, now stands at 3%, so for the six months also it is at 3%.

The slippage ratio, which was at 5.89% as of March 2018 and 0.59% as of June 2018 is now at 0.80%, but for the full six months, it was at 2.42% and now at 1.39% and as regards the credit cost during the current quarter, the total provision is Rs.168.69 Crores whereas in the previous quarter, it was at Rs.193.78 Crores affecting 0.41% credit cost during the June 2018, and now, it is at 0.34%. The credit cost as of half year ended September 2017, it was 0.88%, now it stands at 0.73% and the Provision Coverage Ratio has slightly improved to 57.49%. Cost to Income Ratio is at 46.13%. Return on Asset for the first six months has slightly improved to 0.76% from the last year's 0.71%. NPA addition also for the full six months last year we had addition of Rs.871.85 Crores whereas during the current six months, it is Rs.637.95 Crores. Similarly reduction, last year there was a reduction of Rs.737.74 Crores and this year half year Rs.642.40 Crores and this is by and large the movement in the NPA.

I made a reference to both (i) stress in the portfolio mainly measured by the SMA-2 and (ii) MSME dispensation. This was at around Rs.734 Crores as of June 2018. Now there is a significant reduction in the SMA-2 to Rs.346.74 Crores. In fact, last year for the first six months, our stress i.e. SMA-2 was Rs.1340.99 Crores whereas during the current first six months it is just at Rs.346.74 Crores.

Similarly MSE dispensation, we had around Rs.313 Crores about a quarter back. Now it is at Rs.210.40 Crores. The main reason is we have further streamlined our collection management and we have also finalized on implementing the account wise resolution plan not only for the NPA accounts, but even for the SMA-2 and MSME dispensation accounts and that has given us the desired result during the Q2 and going forward it will be further strengthened and I am not looking for a further increased stress in the pipeline in all probability it will further come down.

Of course, there is no sale of assets to asset reconstruction companies during the current quarter and as a result our security receipt it is at Rs.438.73 Crores as of September 2018. It was at Rs.441.23 Crores as of June 2018 and return on equity has further improved to 10.01% during the first half year of the current season from 8.71% about a year back.

As far as the business numbers are concerned, there is good traction as our deposits year-on-year increased to 12.95%, advances 21.69% growth is recorded whereas in the turnover, it is 16.63% increase is there in the turnover and I said about the improved staff efficiency.

As far as the staff efficiency is concerned, the turnover per branch, turnover per employee and operating profits per branch, then business per employee, business per branch and also establishment expenses per employee, everything there is a significant improvement. In fact operating now the business per branch which was at Rs.126.37 Crores about a year back has improved to Rs.139.53 Crores similarly business per employee, which was at Rs.12.05 Crores about a year back now has improved to Rs.13.98 Crores.

The operating profit per employee, which was at Rs.8.33 Lakhs about a year ago now it is at Rs.8.91 Lakhs and more significantly establishment expenses per employee, which was at Rs.3.22 lakh about a year back now it is at Rs.2.72 lakh that is why the cost to income ratio, which was at 49.17% about a year back has now come down to 46.13%.

Of course, we are on track as far as our KBL – FORCE transformation journey is concerned, so now almost all our branches are acting as lead generators. We have also on-boarded other new channels for the lead generation i.e. the DSA (Direct Sale Associates), then the business associates all of them more than about 150 such agencies have now been on-boarded. This will provide good boost for our retail advances especially the home loans, housing loans, MSME loans and all such things.

In fact last year, this half-year we had seen about 12.31% growth in MSME. Housing has grown by 17.16% and of course car loans by 12.55% and mortgage loan i.e. loan against properties by 40.81% and lease and encash by 13.79%, so these are all the retail growth areas for us during the current quarter and of course we have also further strengthened our collection management under our transformation journey and as far as the IT transformation is concerned, we will be having our own digital center of excellence in Bengaluru very shortly and we will be forming our own subsidiary mainly to manage our contact centers and back office work and all. We have already submitted our application to Reserve Bank of India, so it will be a wholly owned subsidiary to take care of our majority of our back office work.

By and large, the transformation initiative is on track and this is the result highlight for the current Q2. I welcome your questions if any and I am happy to clarify. I am also accompanied by my COO and CFO as well as other senior management team. Over to you now!

- Moderator:** Sure. Thank you very much. We will now begin the question and answer session. Ladies and gentlemen, we will wait for a moment while the question queue assembles. We have the first question from the line of Hrudyam Verma from Augmant Catalyst. Please go ahead.
- Hrudyam Verma:** I actually just wanted to know the deposits that have increased over the past quarter, so how much was from CASA and can you just give me a breakup?
- M.S. Mahabaleshwara:** As far as CASA is concerned during June 2018, it was at Rs.17158 Crores. Now it is at Rs.17298 Crores. Percentage wise, it was constituting 27.35% as of June 2018 and now it is at 27.08%, so in our transformation initiative this is another intervention area where we will be coming out with new methodologies as well as intervention to increase our CASA to a level of around 29% to 30% over a period of two years.
- Hrudyam Verma:** Sir what is our target ROE or ROA from the year-end, any target that you have set in mind?
- M.S. Mahabaleshwara:** We are targeting for 1% and now it is at 0.76%. In fact, as of March 2018, it was just at 0.49%, and we are likely to achieve that number.
- Hrudyam Verma:** Sir just last question. The advances have increased so how much would have been retail and how much would have been corporate lending and was any corporate loans part of consortium lending that we have done in this quarter?

- M.S. Mahabaleshwara:** Yes, as far as the advances are concerned under the multiple banking and consortium advances, we have about the 23% of our total advances under the multiple banking arrangements and about 3.25% of our total advances under the consortium.
- Hrudyam Verma:** Thank you Sir. That is it from my side.
- Moderator:** Thank you. The next question is from Sudhir Mahajan from Entrust Family Office. Please go ahead.
- Sudhir Mahajan:** Good evening Mr. Mahabaleshwara Sir, congratulations on a good result. I am very happy about the increase in the provision ratio from 46% to 57%, but what is the target for the year end?
- M.S. Mahabaleshwara:** Actually we are interested in having about 60% Provision Coverage Ratio, but it all depends on the SS, DS and LS combination of the NPA and our first importance and attempt will be to make provision as per the IRAC norms and in majority of the cases, our advances portfolio is well secured which I have been telling in the past also, so that even if there is a slippage, it would pass through that substandard and DS route and hence, at the initial stage, the provision pressure would not be that much. Added to that, as I have already highlighted in my opening remarks, the pressure in the pipeline is easing and that being the case there may not be much pressure for the provision also for the Bank going forward especially during the remaining two quarters as I see a clear picture of lowering the NPA pressure also in the ensuing two quarters, but of course, we are very closely following these two numbers especially the stress in the portfolio and of course this provision is a consequential thing. We will try our level best.
- Sudhir Mahajan:** Sir the next part is now that you have grown your business at 21%, there will be a shortage of capital adequacies down the line without this kind of growth the NPA problems also will look worse what is the thing on capital you have been looking at? If you now want to get capital at this kind of valuation all the existing shareholders are going to getting?
- M.S. Mahabaleshwara:** Yes, I got your point. For this we have three pronged approach, one is to get as much profit as possible during the current year which would definitely help me to further improve my network. Second one is we have implemented so many capital augmentation measures. One among them is reduction of NPA and to a certain extent, we are successful in that area also. Third one is definitely, we should approach all the interested people and for the current year what we have decided is since we have very good headroom in the Tier 2, we already have plans to go for augmenting the Tier 2 capital through subordinated bond route and in the next year or at end of this financial year at an appropriate time, we may even go for the Tier 1 capital, but we have not yet thought about that. At appropriate time, we will definitely be able to do that. With this Tier 2 capital and our ability to have good profit during the current year, I am sure that whatever the capital adequacy ratio that we are aspiring to maintain we will be able to have that. But as you have rightly pointed out definitely we need capital and at appropriate time with appropriate instrument, we will definitely tap that source.
- Sudhir Mahajan:** Without diluting the existing shareholders value?
- M.S. Mahabaleshwara:** Your suggestion is noted.
- Sudhir Mahajan:** Thank you Sir.
- M.S. Mahabaleshwara:** We will definitely take care of the interest of all the stakeholders. Of course, Bank's interest is paramount and I think our track record speaks for itself.
- Sudhir Mahajan:** Absolute, no doubt about. Sir another last question. Last time you were saying most of your loans are covered at 93% with collateral. Has there been any change in that?
- M.S. Mahabaleshwara:** Slight change is there because we had taken exposure to some of the corporates; they are all AAA rated corporates. If you had gone through our analysis that we had posted in our website, our AAA rated advances, it has increased from 6.16% to 15.11%. Similarly the AA also, which was at 7.77% about a year back, now it has gone up to 8.66%, so this is being the case, as of now around 88% of our total advances are fully secured. The AAA rated advances has gone up and since AAA rated accounts are eligible for around 20% risk weight, as I said earlier, we are making efforts to conserve the capital simultaneously.
- Sudhir Mahajan:** But IL&FS also was AAA rated bond?
- M.S. Mahabaleshwara:** No more.
- Sudhir Mahajan:** No, we had some exposure, that has been totally covered?
- M.S. Mahabaleshwara:** No, IL&FS, definitely when the banks entered into that portfolio, it was AAA and there is a down gradation in the rating which you all know.
- Sudhir Mahajan:** Quantity?

- M.S. Mahabaleshwara:** Yes, my exposure to IL&FS group to three entities we have exposure; this is 0.31% of the total advance and quantum wise it is 156.78 Crores. As of today, this is treated as standard, but one account with an exposure Rs.30.79 Crores, this is under SMA-2, and the rest of the advances are regular but interest servicing for September is not yet done. Till August it is done and we are also closely watching the situation, as and when these developments happen, we will be able to take appropriate resolution methods in tune with the industry.
- Sudhir Mahajan:** Sir two more last questions Sir, one is the CD ratio?
- M.S. Mahabaleshwara:** CD ratio is very much on the expected line, so terminal CD ratio, which was at 75.16% as of March 2018 is now at 78.22%, so we are aiming of around 80% CD ratio in the days to come because the credit growth is on strong footing i.e. 21.69%. What is the second question?
- Sudhir Mahajan:** Sir second question on the investment portfolio. Is it totally covered as on September up mark to market or is there any other?
- Y. V. Balachandra:** The unabsorbed depreciation as of June that is to be covered in the next two quarters, total amounting to Rs.28 Crores.
- Sudhir Mahajan:** Sir, is there anything because the yields in September end had a lot of volatility has there been any other?
- Y. V. Balachandra:** The incremental depreciation is fully provided for. What I was referring to was only the dispensation provided by RBI for amortization of depreciation as of June 2018. As regards the March 2018, you may be aware, we had not exercised that option at all. We had taken fully incremental depreciation as on that date, liability arranging on account of the gratuity investment.
- M.S. Mahabaleshwara:** This September quarter whatever the depreciation was there it was fully accounted for.
- Sudhir Mahajan:** What is the average yield on the government?
- M.S. Mahabaleshwara:** It is 7.01%.
- Sudhir Mahajan:** Thank you Mr. Mahabaleshwara. Thank you Mr. Balachandra.
- Moderator:** Thank you. The next question is from Jai Mundhra from B&K Securities. Please go ahead.
- Jai Mundhra:** Thanks for the opportunity. Sir couple of questions; firstly Sir on this IL&FS exposure, as you mentioned we have exposure to three entities of which one we have already classified into SMA-2, so the rest two entities as the time progress, so they are still below 30 days due is it?
- M.S. Mahabaleshwara:** Just 12 days dues as of now, seven days due. That is debited for September month.
- Jai Mundhra:** Correct, so Sir within these three entities what kind of exposure is there? They have multiple entities in the sense some of them are road assets, some of them are power and one is the parent entity of course, so if you can help us these three entities?
- M.S. Mahabaleshwara:** Parent entity, it is NBFC. There the exposure is Rs.75.54 Crores. Then the transportation network the exposure is Rs.30.79 Crores, which is the account treated as SMA-2. Another one is energy. There the exposure is Rs.50.45 Crores, so all together about Rs.156.78, which constitutes about 0.31% of total advances.
- Jai Mundhra:** Sure Sir. Sir as media suggests that the entire group is under much stress, as possibly as the time progress would it is fair that all these three companies would be coming under SMA-2?
- M.S. Mahabaleshwara:** We are preparing ourselves to the worst eventualities also.
- Jai Mundhra:** Sir any sort of analysis that you would have done in terms of what could be the LGD to transportation network or energy or parent? Which company would be least risky even if the default happens, any sort of?
- M.S. Mahabaleshwara:** I think you have shared that input with us. Let us see. Your question is very much interesting and we have done our homework and at an appropriate time, appropriate measures we will definitely follow, but one consolation point for all of us is all the industry stakeholders right from the regulator they are all working on this and it is our duty to extend full support and cooperation to that type of resolution mechanism.
- Jai Mundhra:** Sir as exposure is standard there is only standard provisioning that we have done right?
- M.S. Mahabaleshwara:** Yes.

- Jai Mundhra:** Sir just another question on the SMA-2 movement that we have shown so there is Rs.600 Crores of deletion/upgradation, so what is that Sir? Have they paid back or have they been categorized to SMA-1 or have they slipped?
- M.S. Mahabaleshwara:** My opening balance in SMA-2 was Rs.734 Crores and of that, during the quarter, there was an addition of Rs.215 Crores to SMA-2 category and deletions from was Rs.602 Crores and out of this deletion, Rs.131 Crores was the slippage to NPA and Rs.428 Crores was the upgradation to SMA-0, SMA-1 and total standard. That means around 72% upgraded from the original stock and about 17.81% slipped to NPA during the quarter and our net amount as of now is around Rs.346.74 Crores.
- Moderator:** Thank you. The next question is from Yash Agarwal from JM Financial. Please go ahead.
- Yash Agarwal:** Sir I had a question on the housing portfolio, which is about 12.3% of your loan book, so what is the nature of this portfolio? It is pure housing loans and is it only in Karnataka?
- M.S. Mahabaleshwara:** Housing loan throughout India.
- Yash Agarwal:** Across India.
- M.S. Mahabaleshwara:** Yes.
- Yash Agarwal:** It is not primarily in Karnataka?
- M.S. Mahabaleshwara:** No throughout India. We have about 11.13% of our total advances under the housing loan itself.
- Yash Agarwal:** Sir what is the yield on this book and what was the growth rate?
- M.S. Mahabaleshwara:** Growth rate has been around 17.66% and housing loan portfolio yield maybe around 9% plus.
- Yash Agarwal:** Sir also we have 15% of our book is NBFC, so incrementally are we lending to NBFCs or we have become cautious on this?
- M.S. Mahabaleshwara:** I have a credit policy and as per that the exposure is fixed at 18%, so as of now we are at 16% and the fresh NBFC lending may not happen, but a quite interesting thing is all these loans under the NBFC as of today except this IL&FS growth all other NBFC exposure there is not even one day default even in the interest servicing, so it is very much regular that is the first point. Second one is, we have taken this exposure for a short period and some portion of that is likely to be repaid in the next six months and another thing is, all this NBFC exposure are getting repriced now since it was linked to the external benchmark and since there is a considerable increase in yield movement as well, so this is the benefit that we are going to get in the Q3 as well as the Q4.
- Yash Agarwal:** Thank you.
- Moderator:** Thank you. The next question is from Rahul Maheshwari from TCG Asset Management. Please go ahead.
- Rahul Maheshwari:** Good evening. I just had one question. During the quarter your NIMs have been on quarter-on-quarter basis it has fallen by 23 BPS and your yield on advances have fallen by 50 BPS. It is only because of the change in the mix from retail to corporates because if we do that thing it shows that your cost of funds has not decreased as compared to the yields on advances, so can you give what is the trajectory because it shows that just in a change in mix your NIMs have faltered down way significant and plus your yield on advances on quarter-on-quarter basis has fallen by 50 BPS that is a huge decline?
- M.S. Mahabaleshwara:** Your observation is correct. The point is, the last few quarters we had one-off interest income especially from the IT income tax paid that interest return was there, that was one of the item. Then as far as the yield on advances and cost of deposit is concerned, both went up by 11 BPS from the previous quarter to the current quarter, but in the cost of deposit what happens this is on the higher base for the full base, but whereas the advances, it is on the smaller base because our CD ratio is 78.2%. That is the reason, but definitely going forward as I said, we are confident that it would be above 3% by FY2019. It is showing the traction in that direction.
- Rahul Maheshwari:** Sir I am not questioning about the 3% of the NIM maintenance, I am just asking or the other way around what is the yield on your corporate and retail part on an average basis?
- M.S. Mahabaleshwara:** The entire yield on advances is 9.40%, entire portfolio.
- Rahul Maheshwari:** No in segment between corporate and retail is the two segments?
- M.S. Mahabaleshwara:** Corporate and retail right now I do not have but we will pass it on to you.

- Rahul Maheshwari:** Does this 50 BPS quarter-on-quarter when your part of your advance will get reprised?
- M.S. Mahabaleshwara:** Yes. That is what I said, especially the corporate portfolio, that Yield on Advances is showing a positive traction and it is going to further increase in the subsequent months.
- Rahul Maheshwari:** Can we expect this corporate as a percentage of your advance, which is 55.8% to increase going forward and your strategy is moving towards more of corporate or it is just a one off kind of thing?
- M.S. Mahabaleshwara:** No. Corporate advances may not increase. Our focus areas is retail and mid corporate and in the retail and mid-corporates especially with our transformation initiative, we are getting a good traction especially in the housing loan and the MSME advances. Besides, we have further strengthened our recovery management, and to share a fact with you, whatever the housing loan that we have lent under the new credit delivery system, about 450 accounts we have considered under that channel and in 160 plus accounts, the recovery has already happened. In all those cases, the repayment is either made on or before the due date or within about five days from the date of the due. So that type of recovery management we have put in place, thus before lending, we have been taking care of all these things apart from the due diligence part, so whenever we are extending credit expansion especially in the retail and mid corporate sector, this is the quality related mechanism that we have already put in place and that is why we are confident even though we grow at a rate of 20% plus in the coming days also, this growth will not be at the cost of the quality.
- Rahul Maheshwari:** 31.5% on advance and just by declining by 8 BPS on your NIMs your NII just have grown by 6.4%, so my only conclusion or reasoning was even if you grow at 20%, but on NII front what would be your guidance that is the main thing?
- M.S. Mahabaleshwara:** We are optimistic that because for the six months even though during this quarter the NII has grown by 6.24%. For the first quarter it has grown by 8.29%, so in all probability it will be in double-digit for the full year. That being the case, we are optimistic and we are confident that NIM would also be at around above 3%.
- Moderator:** Thank you. The next question is from Sneha Ganatra from Subhkam Ventures. Please go ahead.
- Sneha Ganatra:** Sir what is your guidance on the asset quality front? What is the slippage run rate are we expecting or any recoveries are we expecting from the NCLT account also?
- M.S. Mahabaleshwara:** Asset quality front, the guidance is very optimistic and positive. The GNPA, as I said, during the first quarter also I have made it very clear that we should be able to have about 4% GNPA plus or minus 20 BPS to 30 BPS, so that means around 4.3% could be the maximum now it is at 4.66%. Then the slippage also, we should be able to contain because first half year it was 2.42% slippage ratio, now at 1.39% and with the reduction in the stress in the pipeline to a considerable extent, going forward, the slippage would also be contained because all our efforts to recover the dues on or before the due date it is all getting us very good result and in fact we are also making best use of our IT system to ensure that our field level functionaries are contacting the borrowers and ensure that the dues are recovered at appropriate time by enforcing 'day-end check' to the individual branches. If the recovery is not made then, there will be some 'checks' and the branches would have to have approach the higher authority to ensure that 'day-end check' is done by recovering the dues and these are some of the credit discipline that we have been working on and in fact, on many occasions I personally have called many of our top clients to see that their account is maintained at a regular status. Madam that is the result of this reduction in SMA-2 as well as MSME dispensation. As I said, we have account wise resolution plan and going forward, we will be further strengthening this particular mechanism, so I am not seeing much stress in the NPA or in the slippage during the Q3 and Q4 of the current financial year.
- Sneha Ganatra:** Considering what you have mentioned can we assume that slippages run rate would be around Rs.200 Crores to Rs.150 Crores for the next two quarters?
- M.S. Mahabaleshwara:** Depends. But this IL&FS is one thing which we all have to keep it in mind.
- Moderator:** Thank you. The next question is from Sagar Shah from KSA Securities. Please go ahead.
- Sagar Shah:** Good evening Sir. My first question is regarding that the reprising of assets that you told actually that our advances will be reprised from the next quarter?
- M.S. Mahabaleshwara:** This process has already commenced. This process has already started during the last fortnight of September 2018.
- Sagar Shah:** So can you tell that how much something like how many basis points you have increased that MCLR?
- M.S. Mahabaleshwara:** This is varying from 10-basis points to around 70-basis points.

- Sagar Shah:** Due to this actually something like do you expect our yield on advances to go up in the next quarter?
- M.S. Mahabaleshwara:** I am expecting a positive traction definitely. Both costs of deposit as well as Yield on Advance have definitely bottomed out and hereafter, most probably the increase in yield on advance would overtake the increase in cost of deposit that is what our internal calculation reveals.
- Sagar Shah:** In turn our NII income will increase according to you from the next?
- M.S. Mahabaleshwara:** That is the confidence level I have.
- Sagar Shah:** My second question Sir would be on the CASA front, as you know actually our CASA is at 27% actually? Now it has decreased actually if you compare to the last year, so any reasons for the same?
- Sagar Shah:** Even though our branches have increased that is why Sir?
- M.S. Mahabaleshwara:** No, even though our number of clients has increased by 1 million during last one year, we have on-boarded new customers CASA customers about 10lakhs during the last one year and our total customer base has now crossed 1 Crore mark. That is the significant achievement that we have made. Now what is happening is majority of this increase especially during the demonetization period, our CASA had even gone up to 29%. It was at 27.35% as of June 2018 and now stands at 27.08% but quantum wise there is a jump. Percentage wise it has slightly come down. Now under our transformation intervention areas we have identified this also one of our potential areas.
- Sagar Shah:** Yes because if you compare Sir this to the something like to likes of Indusind Bank or any other bank or any other something like a public sector bank where CASA is much above 40% that is why Sir, so there is a lot of improvement to go on here?
- M.S. Mahabaleshwara:** We do not have the luxury of the public sector banks because lot of government related deposits are there in their CASA but, this if you compare with first generation private sector banks this is very much comparable. But nevertheless, we have our own limitations as far as CASA is concerned. Nevertheless, our internal goal is to take it to a level of around 29% to 30% in the remaining two years as part of our transformation exercise.
- Moderator:** Thank you. The next question is from the line of Sangam Iyer from Subhkam Ventures. Please go ahead.
- Sangam Iyer:** Sorry to repeat the question. Sir in terms of reprising what percentage of the loan book is expected to be reprised in the next six months?
- M.S. Mahabaleshwara:** The reprising is happening mainly in the corporate sector, out of Rs.50000 Crores of advances about Rs.10000 Crores is being reprised.
- Sangam Iyer:** Sir since you said it is corporate and predominately we have been increasing our exposure to AA or AAA that is what our commentary?
- M.S. Mahabaleshwara:** Yes that is at company yes.
- Sangam Iyer:** From that perspective and given the backdrop of what was the exposure that we had earlier when we talk about incremental reprising happening to rated accounts would not that lead to dilution in your overall interest if not remaining at the stable level as the best case scenario because better rated corporate obviously will have a lower yield as compared to lower rated corporate?
- M.S. Mahabaleshwara:** No, it is the market dynamism, which we need to understand. When we lend many people felt that we had lent at a lower level, lower interest. At that time what was happening is we had parked this surplus fund in the treasury investment, but currently to the investment I was getting about 50 to 100 BPs higher yield that is why we took that particular decision. Now that decision is paying good dividend for us and at two counts, it is beneficial. One is of course, advances definitely it has helped and the MTM also the depreciation related thing also it has really helped us.
- Sangam Iyer:** Right Sir. Sir my actually question is related to that as well. If I look at this financial year for the first half that we have done so far we have actually grown very strongly? In fact, it was on Q4 of last year that we have started doing at 20% plus kind of a run rate and which is where your investment book has shifted to your loan book, but during the same period when we see this growth your NII is not in line with what your loan book growth is coming in because of multiple reasons, which you did allude to but also to the fact that you are going towards better corporates better rated corporates who are at a lower yield, so what gives us the incremental confidence that the reprising that might happen for better rated corporates would actually result in our NIMs expanding from here on because definitely for every growth that we have been recording for the last three quarters our NIMs have been on a constant decline?
- M.S. Mahabaleshwara:** That is the confidence that I and my entire team are having. Here onwards, it would further strengthen and better position would emerge and in spite of the external adverse situation, this is how we have tried our level

best to insulate our bank from the adverse impact of external things so even under the worst case scenario after IL&FS, I think we have our internal strength to overtake that type of thing.

- Sangam Iyer:** Sir one more thing on IL&FS you said the borrowings done by IL&FS borrowing exposure that they have is around Rs.154 odd Crores right is there any exposure in our investment book that you might have with IL&FS?
- M.S. Mahabaleshwara:** We have about Rs.25 Crores.
- Sangam Iyer:** Sir so overall that Rs.175 odd Crores what is the collateral that you might have with IL&FS just to understand because as somebody asked on that as well for let us say the LGD?
- M.S. Mahabaleshwara:** Pari-passu is there.
- Sangam Iyer:** Finally on the incremental credit cost that you were mentioning so that was excluding anything on IL&FS right?
- M.S. Mahabaleshwara:** As of now we had not incurred any credit cost on IL&FS because it is not treated as an NPA. Only one account is treated that SMA-2 because of the 60 days past due it has crossed. Overall my credit portfolio, credit cost during the September 2018 quarter it is 0.34% only, which was at 0.41% during June 2018, so credit cost is coming down.
- Moderator:** Thank you. The next question is from Gaurav Jani from Centrum Broking. Please go ahead.
- Gaurav Jani:** Thank you for taking my question Sir. Firstly on the NBFC and the corporate front, I believe there would be some overlap between the NBFC and the corporate portfolio right?
- M.S. Mahabaleshwara:** Yes it is.
- Gaurav Jani:** So Sir what portion would that be?
- M.S. Mahabaleshwara:** Right now NBFC exposure as of September is Rs.8323 Crores.
- Gaurav Jani:** Of that how much would that be including the corporate?
- M.S. Mahabaleshwara:** Most of these are corporates only. Entire exposure is also corporate exposure.
- Gaurav Jani:** Sir what I was alluding to is the Rs.10000 Crores that you see reprising that will include the NBFC portfolio right?
- M.S. Mahabaleshwara:** Definitely major from NBFC only.
- Gaurav Jani:** Sure. Just wanted to understand in terms of pricing what kind of uptick do you see in yields from the NBFC portfolio?
- M.S. Mahabaleshwara:** I said now 10-basis points to around 70-basis points.
- Gaurav Jani:** Sir honestly that is a very broader range if you can just tighten the range that will be helpful?
- M.S. Mahabaleshwara:** I do not know how to tighten, you have your calculation. I said this reprising has started during the second fortnight of September. So when reprising has started in each and every account, the lowest jump was 10-basis point and the maximum jump was around 70-basis point and going forward, definitely this 70 may go up and it cannot come down. So that is the level of opportunity that we are having in improving our earnings.
- Gaurav Jani:** Sir probably just one question on a data point basis this quarter what would be the interest reversal because of slippages and the impact on margins because of that?
- M.S. Mahabaleshwara:** Going forward or this Q2?
- Gaurav Jani:** Q2, I mean..
- M.S. Mahabaleshwara:** We will share with you. Right now I don't think we have.
- Gaurav Jani:** No problem Sir that is it from my side. Thank you so much.
- Moderator:** Thank you. The next question is from Vaibhav Barjatiya from H&I Investments. Please go ahead.
- Vaibhav Barjatiya:** Thanks for providing me this opportunity. I think this is important that in last three years from FY2015 onwards a particular line item in our expenditure, which is in operating expenses and within that other

expenditure has grown 3x from Rs.160 Crores to Rs.480 Crores as per our annual reports and this 3x growth in other expenditure is kind of increasing our intermediation cost and putting pressure on ROA, so I wanted to understand that what is driving this and when we can expect a stabilization in this cost? I am looking at annual report schedule 16 within that there is a last line item other expenditure?

- M.S. Mahabaleshwara:** Yes please do me a favor. Please send an email. We will reply immediately.
- Vaibhav Barjatiya:** No problem Sir. Thank you. That is it from my side.
- Moderator:** Thank you. Due to time constraints, we will be able to take one last question. The last question is from the line of Nilanjan Karfa from Jefferies. Please go ahead.
- Nilanjan Karfa:** Thanks for the opportunity. Sir just a question on the MSME book, could you walk us through how the yield on advances on this book has been let us say in the last two to three quarters as well as the asset quality related issues?
- M.S. Mahabaleshwara:** Overall MSME book, it is around 22.86% of our total advances and that is the total MSME and in that, and as I said, with an year-on-year growth of 13.9% and in this, we have an NPA of around 1.13% to total advances and to the sector, NPA percentage is 4.82%. So out of Rs.11625 Crores of MSME exposure that we have about Rs.574 Crores is the NPA as of September 2018. This is as far as the overall MSME advances. Now coming to the MSME dispensation as such, you may be aware that Reserve Bank of India has given by duly considering the importance of the MSME sector they had given certain dispensation that is as per the IRAC norms the 90 days past due concept is there, but there is another 90 days extension is given, so under this category we had about Rs.319 Crores during the last quarter. Now there has been some movement in this particular sector and overall it has come down to Rs.210 Crores, but again in this also, during the quarter, even because this dispensation is open up to March, so we can expect some addition as well as the deletion also, but we are keeping a very close watch on the movement of these accounts in the MSME dispensation list.
- Nilanjan Karfa:** Sir I wanted to understand the trend is these numbers down let us say in the last two quarters and similarly are you facing a lot of pricing problem in this segment?
- M.S. Mahabaleshwara:** As far as MSME, we do not have any pricing problem. In fact, there is a very good scope for all the players in the MSME sector, so depending on our risk appetite we can definitely go for it and of course the institutional mechanism of CGTMSE is there, and by and large, we have a very strong team to handle the MSME depending on our past experience as well. And under the transformation initiative of the BCG, I am also now rolling out a separate credit delivery mechanism for the MSME as being done for the housing loan sector.
- Nilanjan Karfa:** Sir sorry to prolong this question so that DSAs and the business associates that we are adding right are these mainly focused in this particular segment?
- M.S. Mahabaleshwara:** Earlier, we were not having that channel at all and all the business was being sourced from our own staff member through the branch channel. Now a branch is one of the lead generating units and we have tied-up with many DSAs and the builders also so this is now tried for the housing loan sector and the MSME sector. These are the two sectors where we have tied up for the sourcing of the leads.
- Nilanjan Karfa:** Sure Sir if I can just summarize you are saying no pricing pressure as of now and NPLs are mostly contained is what you are saying?
- M.S. Mahabaleshwara:** No pricing pressure. Let's see, there are so many business opportunities like a portfolio buyout etc. we will respond to those things as and when it develops.
- Nilanjan Karfa:** As things stand today you are not afraid of kind of growing into this segment?
- M.S. Mahabaleshwara:** Why we should we? We are in the banking for the last 95 years and we have our centenary year in the year 2024. We are in fact preparing for that.
- Nilanjan Karfa:** Absolutely Sir. We keep on hearing so much negativity on MSME these days so just want to get that assurance Sir.
- M.S. Mahabaleshwara:** No. Those who are not having full control on that portfolio, they may have that type of thing. That is why I have told you all the numbers even what is the pressure there and all, so this is giving us a very consistent return and this is one of our consistent and stable portfolios.
- Nilanjan Karfa:** Agreed Sir. Thank you so much sir for the reply.
- Moderator:** Thank you very much. Due to time constraint we take that as the last question. I would now like to hand the conference back to the management for any closing comments.

M.S. Mahabaleshwara: This Q2 result is very much on the expected lines and I am really satisfied with the performance. I am fully convinced that this has provided a strong foundation for a strong and sustainable growth forward. Almost all the business numbers as well as the earning numbers whatever that we have been committing right from the beginning of this particular financial year, we have been able to walk the talk, but definitely the remaining two quarters are very crucial and myself as well as my entire team of 8000 plus employees because that is why I highlighted how the staff efficiency has also improved. We are all committed to take it forward with the able guidance of Chairman, Shri.P. Jayarama Bhat as well as our Board of Directors also. So by and large, the things are moving in the right direction and of course, we are also keenly watching the industry developments and as and when that type of development would happen, we will be able to respond to those situations. So with this, I would sign-off from this concall. Wishing you all Happy Dasara and Happy Diwali. Lot of festivals nearing and best wishes from Karnataka Bank to each of you and to your family members.

Moderator: Thank you very much. On behalf of Centrum Broking that concludes this conference. Thank you all for joining us. Ladies and Gentlemen you may disconnect your lines.