DCB BANK

General Q & A about DCB Bank - Mr. Murali M. Natrajan, Managing Director & CEO of DCB Bank Limited

The purpose of this general Q & A is to provide useful information about the business strategy and outlook through answers to some of the frequently asked questions. This is not an offer document. Please refer to the disclaimer page in the Investor Presentation for FY 2015 which is available on DCB Bank website as well. This general Q & A may please be treated as an integral part of the presentation mentioned above.

1. Strategy

The business strategy is outlined in Page 34 of the Investor Presentation for FY 2015 which was released in April, 2015. It is also available on our website.

2. Loans Growth Outlook

Our aim is to double the Balance Sheet in 36 to 42 months. The loans portfolio mix is likely to remain the same. Also, we will continue to focus on small ticket loans in Retail, MSME and SME segment.

Due to keen competition, our Corporate loan book is experiencing an unexpected fall in the Q1 FY 2016. In both Corporate and MSME / SME we continue to have a cautious approach given present market conditions. We continue to make steady progress on Retail and AIB. We have also invested in enhancing frontline capacity and branch network and believe that proper execution will help us to build growth momentum. Overall, the first two quarters are likely to be sluggish in FY 2016.

3. NPA

At the moment, Mortgages, CV, Gold, MSME, SME and AIB portfolios seems to be performing well. The delinquencies and NPAs are within our tolerance limits. In the last few years at any point in time, for various reasons, two or three Corporate loans have shown signs of stress. So far, we have been managing these accounts and ensuring repayments. In the last quarter of FY 2015 we had one large exposure which became NPA. It is possible that one or two large exposures may slip into NPA in FY 2016 as well.

Timely identification of stress, reducing exposure, exiting difficult accounts, redefining risk appetite, etc. are regular activities performed by the risk team in order to maintain portfolio quality. We also have a strong recovery process.

We are hopeful of maintaining overall portfolio quality in FY 2016.

4. Restructured Portfolio

Our Bank is not a member of CDR. We are selective in restructuring loans. At at March 31, 2015, the restructured standard portfolio is Rs. 58.46 Cr. comprising of 8 accounts.

5. NIMs

There is a lot of pressure on NIMs. We have a strong focus on CASA and Retail deposits. We are ensuring diversified loans portfolio. We have been successful in meeting Priority Sector Lending targets. However, we are somewhat short in meeting Direct Agri and Weaker Section sub-targets. This results in subscription to low yielding RIDF / NABARD long term bonds. We are actively managing sources of funding so as to keep Cost of Funds within acceptable range. In the near term, we are expecting pressure on NIMs. However, if over time, Term Deposit rates starts to decrease, we may be able to recover some part of the NIM reduction.

6. Non Funded Income (NFI)

In terms of strategy execution, we have a lot of scope for improving fee income. We have more exposure to Retail and MSME / SME and limited exposure to Corporate loans therefore, we have limited large ticket fee opportunities. Having said that our aim is to grow fee income by 12 to 14% per annum. The focus is on granularity. We have already stepped our efforts to train frontline staff on bancassurance, third party products distribution, FX and trade. We are confident of improving the momentum in the coming months.

7. CASA Ratio

We have been able to grow CASA deposits at 14 to 16% per annum. However, Balance Sheet / Total Deposits growth is much higher than CASA deposits growth. This is resulting in reduction in CASA ratio. We expect CASA ratio to go down further before bouncing back to 23 to 25% level in 2 to 3 years. This is expected when the new branches starts to mature and attain higher momentum.

8. Branch Network and Headcount

At present we have 154 branches. Our plan is to open 25 to 30 branches every year subject to Cost / Income ratio remaining in control. As per the current business model, branches are expected to break even in 18 to 22 months depending upon size and location.

We have a full range of products. Therefore, we intend to make available in all the branches all products applicable to the catchment area.

The main states for branch expansion are likely to be Andhra Pradesh, Chattisgarh, Delhi, Karnataka, Gujarat, Haryana, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan and Tamil Nadu. The branch expansion would be in accordance with the Reserve Bank of India (RBI) guidelines. We are targeting to reach around 300+ branches in about 4 years.

Around 12% of the branches installed so far are not performing as per plan. Usually, the main reason for under performance is instability in branch team, local infrastructure issues, process delays etc. We are constantly putting corrective actions in place to rectify the situation.

DCB headcount as at March 31, 2015 stands at 3352. Based on branch expansion plans, the headcount is expected to increase by 300 to 500 every year.

We are making appropriate investments in frontline technology to improve staff productivity and customer experience.

9. Cost / Income Ratio

Cost / Income ratio is high and it is our number one challenge. Much of Cost / Income ratio problem is because of the size of our Balance Sheet. We are likely to grow our Income faster than Costs growth therefore, we expect Cost / Income ratio to steadily decrease over time. We are investing in frontline capacity and branch network. This is adding further pressure on Cost / Income ratio. We are confident of achieving Cost / Income ratio of 55% in approximately 2 years.

10. **ROA / ROE**

In 24 to 30 months, we are targeting ROA of 1.30% and ROE of 14 to 15%. In FY 2016, full Income Tax rate may be applicable which will depress the Profits After Tax for FY 2016 and affect the ROE / ROA for FY 2016.

As we increase Balance Sheet size, improve profitability, Cost / Income ratio (largely through cost productivity), we are targeting higher ROA and ROE. Of course, we need to ensure good portfolio quality as well.

11. Payment Banks / Small Banks / New Banks

The banking landscape may change substantially in the coming years. We need to be prepared. We have to improve our technology and customer experience. We need to have faster seemless delivery. We have to work hard to retain talent. We also have to concentrate on product innovation and customer connect. Otherwise we will face more pressure from both new and existing players.

At the same time, it may not be easy for the new entrants to compete with well entrenched existing players.

Payment Bank is a new and untested concept. It may take a while before Payment Banks become profitable. They may not have difficulty in acquiring large number of customers. Payment Banks need to be fully geared to deal with AML / KYC risk and operational issues.

12. AKFED Dilution

After the recent capital raising, AKFED plus affiliates hold 16.38% of Bank's equity. As per the road map submitted to Reserve Bank of India (RBI) earlier, AKFED plus affiliates stake is to be reduced to 10% by

March 31, 2014. We have represented to RBI seeking extension of time for dilution of promoter stake.

13. Capital Raising

We raised Tier I Capital of Rs.250 Cr. through QIP in October, 2014. Our capital position is strong. We may not require fresh Tier I capital infusion for another 24 to 36 months. As and when needed, depending upon market conditions, we may first explore Tier II and AET1 options to increase capital.