"Development Credit Bank Conference Call"

July 19, 2010

Moderators:

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Moderator: Ladies and gentlemen, good evening and welcome to the Q1 FY 2011 conference call of Development Credit Bank. As a reminder, for the duration of this conference, all participants will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should need anyone need assistance during this conference they may signal the operator by pressing "*"then "0" on your touchtone telephone. Please note that this conference is being recorded. At this time I would like to hand the conference over to Mr. Murali Natrajan, MD and CEO of Development Credit Bank. Thank you and over to you sir.

Murali Natrajan: Good afternoon everyone. In the first 10 to 15 minutes let me just give you a brief background and highlights of our performance for first quarter of this year and then I will be open to questions. Let us first talk about the headlines. The loss for the quarter was Rs. 2.9 Crores. This compares with the previous quarter that is the fourth quarter of the last year loss of Rs. 8.2 Crores and first quarter last year loss of Rs. 35.3 Crores. So consistently we have been improving our performance and reducing our losses. We believe that if we continue to improve the P&L dynamic and the Balance Sheet as we are doing, we should be able to come to a positive number for this year. Our strategy as I have explained in the previous calls and our meetings with some of you is to grow our CASA, focus on Retail Term Deposits, diversify our loan portfolio in home loans, SME, Micro SME, Agri, and Mid Corporate Banking. In line with that strategy we were able to grow CASA in absolute term by Rs.149 Crores and our CASA ratio stands at 36.0%. Our stated strategy is that we should always keep CASA above 30% and that is the goal that we are pursuing, so we are doing better than our target. In terms of Retail Term Deposits we continue to grow our Retail Term Deposits. We have had the benefit of reduction in cost of

Retail Term Deposits as we had picked up certain high cost deposits in the year 2008. I expect in the next three-four months or so those benefits would stop accruing to us, so the cost of fund benefit that we are seeing would stabilize in about three to four months time.

Home loans portfolio, we are able to grow on a month-on-month basis. Similarly we are continuing to do well on SME and Micro SME. All in all we are able to pursue growth in the chosen areas. However, we still have some of the older portfolio, which is Unsecured Personal Loan, Commercial Vehicles, etc., which we are running down, so net of run down our portfolio growth has been moderate this quarter, but I expect that by end of second quarter or by end of third quarter we should see a decent growth in our loan book. Our own target is growth of about 20% this year, both on deposits and advances. In terms of operating profit we had an operating profit of Rs. 22 Crores this quarter as compared to Rs. 19 Crores in the fourth quarter of last year. The provisions were at Rs.25 Crores. I am happy to say that the provisions for the retail portfolio especially personal loans are consistently coming down and we should be able to see a lot more reduction in this provision in the second / third quarter of this year because we have already provided almost 90% of the NPA in Unsecured Personal Loans. The coverage ratio that is expected by Reserve Bank of India by September 2010 is 70%. I would like to say that our coverage ratio at the moment is 75.2%. The gross NPA also has come down marginally to 8.5% and the net NPA has dropped from 3.1% to 2.5%. We are in a strong capital position. Our capital adequacy under Basal II is at 13.8% and most of the capital is in Tier I. We have an approval from the Board of Directors as well as the AGM to issue Rs. 150 Crores through QIP route. If everything goes well we plan to complete this by December this year.

One other news I would like to share, which you might have seen in our press release. We have been given two branch licenses by Reserve Bank of India, one in a place called Netrang (Bharuch District), it is a rural branch and another place called Mandvi (Surat District), it is a semi-urban location. Both are in Gujarat. We see this as a positive development because it has been quite some time since Reserve Bank of India has given any approval at all for branch licenses. We believe that if we continue to perform well in our financials and continue to improve the bank. We should be able to obtain few more licenses from Reserve Bank of India in the coming months, but we will wait and see how that works out for us.

All in all what I want to say is that we are continuing to improve our Balance Sheet and P&L and just to repeat myself if we perform like this, stick to our strategy and have the discipline of executioning like the way we are doing we hope to come to a positive or a profitable zone by third quarter of this year. Those were the highlights that I wanted to share with you. I am open to questions.

Moderator Thank you very much Sir. Our first question comes from the line of Abhishek Kothari from Way2Wealth Securities. Please go ahead.

Abhishek Kothari: What was the duration of your SLR portfolio?

Murali Natrajan: I am joined by Mr. Bharat Sampat. Bank's CFO as well as Mr. Rajesh Verma, Head of Treasury. They will just answer that question if you give us a minute.

Bharat Sampat: Modified duration of HFT portfolio is 3.00 and HTM is 5.08.

Abhishek Kothari: Could you also share with us your other income breakup?

Bharat Sampat: Other income major components we have Bank Guarantees Rs. 1.5 Crores, Processing Fees is Rs. 3.0 Crores, Insurance Commission Rs. 2.7 Crores, Commissions, Exchange and Brokerage total of Rs. 15.6 Crores, Profits on Exchange Transactions Rs.1.8 Crores, Gain on sale of investments Rs. 8.6 Crores. Out of the gain on sale of investment as allowed by Reserve Bank of India we can transfer one time from HTM, which we did in this particular quarter that is the one-time of about Rs. 4.9 Crores this quarter, but it is every year we have that opportunity, it just happens to be in this particular quarter.

Abhishek Kothari: Sir, what was the restructured account amount wise and what was the slippages experienced within the quarter?

Murali Natrajan: We have a very limited restructured account, to be honest I am not carrying that detail, but I can mail you separately. We do not have too many restructured account and when we look at our restructured I do not think there has been any slippage, if there has been any slippage we have already provided for that in the corporate.

Abhishek Kothari: Sir, out of this 75.2% provision coverage ratio, how much was from technical-write offs?

Murali Natrajan: No technical write off (during the current quarter). We have only one corporate loan that we have provided that we had a written off in the last quarter of last year. So this is all without, I mean, (except for) just one account, which we took with the approval of the audit we took a write off which was of course fully provided for.

Abhishek Kothari: What was the risk weighted asset at the end of the quarter?

Murali Natrajan: Risk weighted asset was approximately Rs. 4,618 Crores under Basel II.

Moderator: Thank you. The next question comes from the line of Naga Deepika from Capital Market. Please go ahead.

Naga Deepika: This is regarding the Base Rate system. We have announced 7.75% of base rate; going ahead how do you see the proposition of loans to be, how was the housing loan when it was in BPLR system and how would be that in the base rate system and how are you trying to tackle, because there are news that SMEs can have low, good amount of reduction in interest rate, how are you tackling this situation now?

Murali Natrajan: I am going to give you some answers, but I hope they are the answers that you are looking for. First of all, we have created our base rate based on a suggested methodology, it is not compulsory to adhere to that methodology but there was a suggested methodology by Reserve Bank of India. So we took that process of taking three-month interest rate added certain volatility, looked at our CASA proportion, looked at the SLR and CRR and unallocated overhead plus profit margin so that is how we came to short-term base rate of 7.75%. What we planned to do is if we get any longer tenure loans, we will add tenure premium and product specific cost and credit loses to that and quote our rate, so our rate is at 7.75% at the moment. It is too early, the market is, I think still grappling with the impact of base rates. As of today, I have not seen any issue on that. So far as Home Loans are concerned almost every loan that we had given since we started Home Loans in September, 2009 is above the base rate, in fact some of the loans are well above the base rate, so I see it like this that base rate will actually help in bringing some amount of transparency to the Home Loan customers, but the rest of it would be dictated by the competition. Regarding SME, if an SME customer is rated well he is approached by several banks for facilities therefore I think there is in-built market system whereby they are able to get better pricing. SMEs who's financials are not good or whose business experience is not enough, they tend to pay higher rate and I think that should be expected because there is a risk element to it, which is priced by the market, so very early to comment on base rate, but these are some of the things that I am observing at the moment.

Naga Deepika: What is our last BPLR?

Murali Natrajan: Our BPLR was about 15% but we always used to quote BPLR – 4% or 5%like that.

Naga Deepika: Right. Is there any difference between the home loans before base rate and after implementation of base rate?

Murali Natrajan: We have not changed our home loans rate after base rate, we were quoting anywhere between 8.5% to 8.75%, however, if there are customers who are of a risk profile where we need to add a little bit more risk premium we would probably even quote say 9% or 9.25%, so we have not made any changes to that, that I think is somewhat dictated by the market competition type of things.

Moderator: The next question comes from the line of Amit Ganatra from Religare Asset Management. Please go ahead.

Amit Ganatra: What is the current size of the Unsecured Personal Loan and CV/CE portfolio book?

Murali Natrajan: Approximately Rs. 60 Crores is Unsecured Personal Loans, I expect this to run off in the next few months and CV/CE will be about Rs. 250 odd Crores.

Amit Ganatra: Okay, what is the overall size of the non-funded book in the form of LCs and guarantees?

Murali Natrajan: Guarantees is about Rs. 500 Crores and acceptances, etc., is about Rs.255 Crores. LCs is Rs. 255 Crores approximately. We have usually about Rs. 1000 Crores in non-funded, which attract capital.

Amit Ganatra: Yes, so that explains the risk weighted assets being higher than the…

Murali Natrajan: It averages around Rs. 900 to Rs. 1,000 Crores.

Amit Ganatra: Just wanted to reconfirm basically profit on sale of investment is 8.6 Crores out of your total other income of…

Murali Natrajan: Profit on sale on the specific item of transfer from HTM to AFS is Rs. 4.8- Rs. 4.9 Crores, the balance is usual trading income of Treasury.

Amit Ganatra: Right. From an understanding perspective, basically the provisioning amount on quarter-on-quarter base is constant, but it seems that it has largely gone towards increasing the coverage ratio rather than actual slippage happening in the quarter, the total provision coverage ratio is already 75%, so incrementally if the slippages are actually low, then just to understand based on the current run rate you should have turned profit in second quarter itself but you are still guiding for third quarter, so it just…

Murali Natrajan: I want to turn profitable in first quarter itself so the intention is to turn profitable as soon as possible. The coverage ratio is like this, see in case of Unsecured Personal Loans as per RBI norms you have to provide 100% in 455 days, so the fresh slippage may not be there, but within the slippage if there is an aging that is going on we still have to provide.

Amit Ganatra: Okay, so basically coverage ratio can still go up may be one more quarter?

Murali Natrajan: Yes, it will go up one more quarter and there is nothing wrong with that because at a later point in time hopefully if our collection efforts continue to be good, some of it should come back as well.

Moderator: Thank you. The next question comes from the line of Jaiprakash Toshniwal from Taurus Mutual Fund. Please go ahead.

Jaiprakash Toshniwal: My question is on the largest promoter shareholder, what is the time line to reduce the stake and what is the process?

Murali Natrajan: Okay, let me answer this. We are allowed to keep this 23%, in fact we were allowed to keep this 26%, which was before the QIP that we did last year up to March 2012, from March 2012 to March 2014 we have been allowed to reduce that to 10% and no new capital issue can be subscribed to by the promoter whether it is Rights or QIP or whatever, but we are already at 23% as we did QIP last year of 81 Crores. If we do one more QIP by December of Rs.150 Crores perhaps another 4% to 5% would be dilution in the stake and the process is basically if you issue fresh capital we will dilute the stake to 10%. There is no discussion or there is no board discussion or any intention of the promoter to sell their stake at the moment if that is what the answer you are looking for.

Jaiprakash Toshniwal: Okay sir, thanks.

Moderator: Thank you. The next question comes from the line of Ramnath V from Birla Sun Life Insurance, please go ahead.

Ramnath V: I missed on the data point in terms of the Personal Loan portfolio that you gave what is the current outstanding personal loan…

Murali Natrajan: Approximately Rs. 60 Crores is outstanding Personal Loan, the rest is all basically NPAs in which we are doing recoveries. Rs. 60 Crores is a good book that would run off in due course of time may be in about a few months.

Ramnath V: In terms of coming back to business growth when are you expecting the pick up in the entire loan portfolio to start happening?

Murali Natrajan: Loans are growing, we did grow in Q4 of last year as well as this year, but we have to deal with the rundown portfolio as well, which we have consciously kind of exiting. I expect our loan portfolios to deliver at least 18% to 20% growth over March 2010 this year and I think by second quarter or third quarter we should see growth in our loan portfolio.

Ramnath V: This Rs. 60 Crores of portfolio is something that will run off, but…

Murali Natrajan: Rs. 60 Crores is there plus Commercial Vehicle / Construction Equipment is there, and there may be one or two term loans or something in corporate, which may be getting fully repaid, and there are some moving parts in the Balance Sheet.

Ramnath V: Sure. You also expect to get out of the CE and CV vehicle?

Murali Natrajan: We have already stopped sourcing Commercial Vehicle, Construction Equipment almost two years ago, at the moment there are no plans to re-enter the business if it is there I will definitely come back to explain that.

Ramnath V: What is the outstanding amount of CV/CE that you have got?

Murali Natrajan: Commercial Vehicle / Construction Equipment is about approximately Rs. 250 odd Crores.

Moderator: Thank you. The next question comes from the line of Rajatdeep Anand from ICICI Prudential Life, please go ahead.

Rajatdeep Anand: What was the number for additions to gross NPA for Q1 this year?

Murali Natrajan: The gross NPA number went down from Rs. 319 Crore in fourth quarter to Rs. 314 Crore.

Rajatdeep Anand: So that can be on account of write-off or upgrade or fresh addition…

Murali Natrajan: I do not recall any fresh addition in the Corporate loan book. Our SME book if there has been any addition it has been very minor addition. There has been no addition in terms of Retail book. Because Retail book

NPAs have stopped accreting for almost now two or three months if I am not mistaken, so most of it is either coming from upgrade or recovery and in case of unsecured personal loan whenever we do some kind of a settlement on account-by-account basis, the amount that is sacrificed is taken out of the gross NPA.

Rajatdeep Anand: So incrementally there is zero….

Murali Natrajan: Negligible increase on account of one or two SME loans, if at all.

Rajatdeep Anand: I saw on BSE that you have been allowed to open two more branches, so how does the discussion with RBI usually progress by when would you know that how many licenses you have for FY 2011?

Murali Natrajan: Very hard for me to answer that question. I am extremely happy that Reserve Bank of India has allowed us to open two branches. We see that in positive light as we improve our performance of the portfolio, actually what happens is that I think normally branch licenses are based on bank's performance and if the bank has any ownership issues that also needs to be resolved. We believe that by giving a roadmap of dilution of promoter's stake to 10% by March 2014 from our point of view we have resolved the ownership issue. As we improve performance, I do expect RBI to consider some licenses. What timeframe and all very, very hard for me to tell you.

Moderator: Thank you. The next question comes from the line of Emmaneul Elango from Kotak Mutual Fund. Please go ahead.

Emmaneul Elango: I just wanted to understand out of your total book how much will you just let it wind down as of now? How much is left?

Murali Natrajan: Approximately Rs. 60 Crores of Personal Loan, and about Rs. 250 Crores are Commercial Vehicle & Construction Equipment, is being consciously run down.

Emmaneul Elango: Okay, so all this is featured in your Retail Banking split of assets that you have given in your presentation?

Murali Natrajan: Yes, correct.

Emmaneul Elango: So around Rs. 300 - 310 Crores of assets you expect to run off for the next two to three months. In the next two to three months will it be over or will it?

Murali Natrajan: The next few months I said.

Moderator: The next question comes from line of Sneha Kothari from KC Securities. Please go ahead.

Sneha Kothari: What is the outlook on your NIMs and cost to income ratio, what is your target for FY2011?

Murali Natrajan: Shall I answer the cost income ratio first?

Sneha Kothari: Yes fine.

Murali Natrajan: In 2008-2009 our cost was approximately Rs. 240 Crores, in last year we cut down approximately Rs. 40 Crores from our cost, so we were at about Rs. 200 Crores, if you see our first quarter cost it is about Rs. 51 Crores suggesting that we have not grown our cost dramatically at least in the first quarter and we do not have any intention of letting this cost be more than 2-3% over the previous year, so we are managing the total cost. At the same time, we are focusing on growing our Balance Sheet and income, our problem now seems to be more on the size of the Balance Sheet as opposed to the cost that we have, so at this moment the cost income ratio does look very high at about 70% or so, the intention of the management team is to bring it down below 60% in two to two-and-half years time by consistently growing Balance Sheet and income, at the same time keeping a check on cost except for sales teams we do not plan to incur cost because we have capacity in operations we have capacity in credit, we have capacity in collections and so on, so that is how we are managing the cost, so my challenge is more on growing the balance sheet size at the moment. Now the first question on yours NIM, our intention is to keep CASA ratio above 30% currently we are happy that we are doing better than that, we are at 36%. Our NIM for the quarter was about 3.1% but as we grow the balance sheet I do think that our NIM will probably range from 2.7-2.8% because some of the benefits of the high cost deposits that are being reprised would not be accruing to us after three to four months, so I would look at the NIM at more like 2.7 to 2.8%.

Sneha Kothari: What is the proportion of your high cost deposit to the total deposits?

Murali Natrajan: What is your definition of high cost deposits?

Sneha Kothari: Above 5 Crores?

Murali Natrajan: Maybe I will answer it like this, two years ago 50% of our deposits were in Treasury and Wholesales Corporate Deposits, now 80% of our deposits are in CASA and Retail Term Deposits, so only about 20% are in Treasury and Corporate Deposits. In terms of high cost, I believe that most of our high cost deposits would be, if at all, in Retail area because when you raise Term Deposit at say 9-8.5% one to one-and-half years ago, those will take time to run off, so I do not believe that in our Treasury or Corporate Deposits we have any high cost deposit.

Moderator: Our next question comes from the line of Abhishek Kothari from Way2Wealth Securities. Please go ahead.

Abhishek Kothari: Sir, just a follow-up. What is the Other Income growth target seen for the year?

Murali Natrajan: There are some challenges in Other Income, so first of all let me tell you that like a bancassurance that we were doing there are changes that have happened in the IRDA policy, so that all would have to fall in place by August, September. Our intention is to grow Other Income this year by about 10%, but I would have a much clearer picture of this because a lot of initiatives and progress in terms of remittances increasing LC business, bank guarantees, improving penetration of insurance cross-sell in the CASA base and so on, so I would have a clearer picture in about one to two quarters but our intention is to grow it by 10%.

Moderator: The next question comes from the line of Jaiprakash Toshniwal from Taurus Mutual Fund. Please go ahead.

J. Toshniwal: Just wanted to understand your feeling about the Base Rate how it is going on and what is your sense you are getting from the market?

Murali Natrajan: I am not too sure that a complete clarity has emerged on Base Rate. I think fundamentally all the banks have declared their base rate and you of course have that information on what are the ranges of base rate. I always felt that base rate impacts primarily two types of lending, one is short term corporate lending, and another is the home loan. I do not believe that it would significantly impact SME or even term loans of either companies or SMEs or whatever, so far as home loans are concerned most banks had rates above their base rate in terms of home loan we also had our home loan at about 8.5-8.75% so if I have made any change to my rate, that would depend on competition. Regarding short-term corporate loans, I do see some run off in at least our portfolio because of base rate, but it is somewhat too early to say.

Moderator: The next question comes from the line of Deepak Radhakrishnan from Unifi Capital, please go ahead.

D .Radhakrishnan: My question is on the road ahead, what is the major challenge that you face, is it in terms of people or is it in terms of technology and how do you plan to overcome it?

Murali Natrajan: Fundamentally the challenge that we face today is that our Balance Sheet is small, therefore the earnings are small and while we have got good control over the NPAs and the provisions etc., the absolute operating profit is still small, so if there are some unforeseen NPA or provision then the absorption capacity is at the moment low, so that is the fundamental challenge, so our aim is to grow our Balance Sheet in a cautious and systematic manner, well diversified portfolio with secured lending so that we improve the earnings potential of the Bank and improve the loss absorption capacity. That is basically the first task that we are dealing with.

D. Radhakrishnan: Right, but what is the major challenge that you would face in doing that?

Murali Natrajan: In terms of technology we are using modern technologies, e.g. we use Infosys Finacle, and we have very high quality systems across the spectrum so I do not see that as a big challenge. I think people continue to be a challenge in the industry, so we also face our share of challenges in terms of losing front line to other banks or other financial institution. We have not had any challenges in terms of attracting management team or improving management quality. Frontline definitely there are challenges in terms of growing the business, but we have put together some good strategies in terms of how we will attract, what kind of scorecard we will administer, what would be the incentive plan and we are meeting with some success, so I do hope that we will be able to meet those challenges as well.

Moderator: The next question comes from the line of Kailash Gandhi from Wallfort Financial Services. Please go ahead.

Kailash Gandhi: Just wanted to understand your Personal Loan portfolio, basically the understanding is more about the Personal Loan scenario after the base rate, will it be coming down, and will the Personal Loan hold outs be positively impacted in any way by this base rate?

Murali Natrajan: We do not do Personal Loans. We left Personal Loans business in August, 2008. We do not intent doing Personal Loans, at least that is not part of our strategy for the next 12-18 months because for a Balance Sheet of our size we do not think that Personal Loan is the right thing to do, having said that what I understand from the market is that base rate has not had any impact on personal loans, they used to be at 14-18% and they probably are continuing to be in that range.

Kailash Gandhi: Okay fine. So you mean to say that the MSME and the personal loans people who are the customers basically will not be in anyway impacted because what I am trying to understand is the impact of the base rate because of the cost and the profit part which has been included to it, in anyway are they guiding on these fronts to the banks?

Murali Natrajan: Yes, it is hard for me to guess what RBI would be guiding, if you were asking about SME and MSME the way it works is if smaller SMEs who inherently have a little higher risk in terms of their business, usually are not able to get rate less than say 12% from most banks, but if it is good performing SME with let us say Rs. 50-70 Crores of annual turnover they do have the ability to kind of, because of their strength in their balance sheet, they are able to get better rates, so as far as the base rate is concerned, my belief is that it is only impacting at the moment short-term corporate loans and if at all home loans, I do not think SME, MSME are impacted at that moment.

Kailash Gandhi: Okay, so the sub PLR lending is what is actually being curbed as of now?

Murali Natrajan: There is no lending possible below the Base Rate.

Moderator: The next question comes from the line of Jigar Walia from OHM Stock Brokers. Please go ahead.

Jigar Walia: Sir, looking at the operating cost, we have been maintaining it at Rs. 51 Crores a quarter but just looking in to the breakup of it, employee cost increased sequentially significantly, so last quarter there was a pretty lower number and this quarter is there a bonus element or is there something to read in to the previous number?

Murali Natrajan: Yes there are two important items, because of the losses that we suffered in 2008-2009 for a very long time we were to unable to give salary increases or bonus to much of our employees, as situation started improving in the fourth quarter from a retention point of view as well as from a point of view of rewarding the good performance in our team, we did increase salaries and we did have some bonus payout so that is already factored into our first quarter, on top of it we had a lot of staff in contract who were part of the operating expenses, not staff, so we regularized all of them and brought them into staff cost, so those are the changes that are showing in our staff cost.

Jigar Walia: Okay great, but overall will you be able to maintain it at around 200 Crores or a little bit high at 5% ?

Murali Natrajan: Our intention is to keep it at a level of 200-202 Crores.

Jigar Walia: Can we have the breakup of the portfolio in terms how much is Corporate, how much priority, and SME?

Bharat Sampat: Retail total is Rs. 843 Crores, SME + Micro SME is Rs. 628 Crores, Corporate is Rs. 1,194 Crores, and Priority Sector that is Agri, Micro Finance, Rural Banking is Rs. 814 Crores.

Jigar Walia: How much is the mortgage?

Bharat Sampat: It's Rs. 470 Crores.

Moderator: Ladies and gentlemen, that was the last question. I would now like to hand the floor back to Mr. Natrajan for closing comments.

Murali Natrajan: Thank you very much for your patience. If you have any follow up questions or if you would like to meet the management team or myself please feel free to contact Meghana who is our Investor Relationship Head or Bharat Sampat who is the CFO. We will be more than happy to meet with you and answer your questions. Thanks for your time. I really appreciate your patience.

Moderator: Thank you very much. On behalf of Development Credit Bank that concludes this conference call. Thank you for joining us and you may now disconnect your lines. Thank you.