"DCB Bank Limited's Q2 FY'23 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to DCB Bank Limited Q2 FY'23 Earnings Conference Call. Joining us on the call today are Mr. Murali M. Natrajan – Managing Director and CEO; Mr. Satish Gundewar – CFO; Mr. Ajit Kumar Singh – Chief Investor Relations Officer, Mr. Praveen Kutty – Head Retail Banking.

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 call, 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. Murali M. Natrajan. Thank you and over to you, Sir.

Murali M. Natrajan: Thank you. Good evening, all of you. I am speaking to you from the boardroom of our corporate office. I have here in the boardroom. Mr. R Venkattesh, who Heads our HR, Technology and Operations, then we have Mr. Praveen Kutty, who is the Head of our Retail Banking; then we have S. Sridhar, who's the CRO of our Bank, then we have Satish Gundewar, who's the CFO, then we have Ajit Singh, Head of Treasury and Investor Relations, then we have Meghana Rao, who's Head of Operations, and then also some of our key staff.

We've had a very good quarter once again, and we are on track, I would say to double the balance sheet between three to four years. When I analyze our performance over the last few years, what I see is that the first year when we started this journey around 2008, 2009, we had to kind of stabilize the balance sheet. From 2010 to 2020, we grew at a CAGR of the loan book at about 22% for 10 years. Then we had about two years of COVID where we have grown at an annual rate of 7% odd.

Now when you look at the growth in comparison to last year, we are at 18% already. And we are confident, the kind of investments that we are doing in the front line and the depth we are creating in our product, process, systems, we should be able to double our balance sheet between three to four years.

The second important point is while the slippages are still slightly high, I would say, looking at the collection efficiency, which is pretty much back to COVID-19 stage. And then if you look at our upgrades and recoveries, we are doing quite well. Unfortunately, some old corporate accounts slipped this quarter. I would not say that it was not expected, but when accounts go into NCLT, it takes a long time for resolution, and these loans have been with us for more than 10-years, and they've had some challenges recently and then has gone into NCLT. So, the resolution is taking time.

But having said that, the retail portfolio, gold loan, recoveries and upgrades are doing extremely well. Even the repayment from our restructured book, as we never restructured any unsecured loans, very, very miniscule amount of unsecured loans we restructured. So, the payment that we are able to get from the restructured book, our collection efficiency is also improving. So, we are pretty confident about our portfolio. We are obviously getting the benefit of lower provisions.

What has been a bit of a surprise for us this year is that we generally have a very decent flow of income from PSLC, but the rates of PSLC have been low this year. So, therefore, we are having lower income in PSLC than last year than our expectation. But our other income, like the core fee, income processing fee, third-party product distribution, all that is doing very well and compensating for some of the shortfall in that.

So, balance sheet on a year-on-year basis have grown at 13%. Deposits have grown at 16%. We are doing quite well on CASA; it has grown by 35% and we are almost close to 30% on CASA ratio. Loan book like I said the growth is 18%. Our net interest income has gone up by 27%. NIM is at 3.88. However, I would like to again guide that our approach is 365 to 375 basis points. The deposit rates are going up. And there is a limit beyond which you can't keep passing on the cost to the customer. Of course, we are following the EBLR and MCLR method as prescribed by RBI.

With respect to our operating cost, it is going up in line with the investments we are doing. As far as we are concerned, we have no surprises that we want to build a frontline capacity. So, however, on a year-on-year basis, I don't expect the cost to increase the way it has increased this year, over last year, in the next year. So, we are creating a platform for us to build a bank to be able to keep doubling every three to four years.

Our headcount has reached a level of 9,443. Again, it is as per our plan. And what we are finding is that our disbursal volumes are also going up in line with the frontline capacity that we are building, and you can see the disbursal volumes in our Investor Presentation, which has grown by 49% over the previous year same thing and quarter-on-quarter it has also grown. Again, the growth is led by mortgages, within that home loans, KCC, tractors, gold loans also have done well. We are doing reasonably well in co-lending and spreads as well.

We have already talked about the provision. Cost-income ratio is high at 64, but our target is to go below 55%. It will take us some three to four quarters, but we are on track because we are building the volumes. And as the lower volume builds up, we don't expect the same level of investments in frontline is required for us next year. However, the current year investment starts to kind of deliver result which I've already shown you that disbursals are really stepping up which is quite good. The demand is also quite robust. Both gross NPA and net NPA has come down and we expect to continue to improve this and coverage ratio has also gone well about 70%.

We are strong on capital. I would like to remind that current year profit is not included in our capital computation. ROE is improving. Again, our target is to reach 14% And then, ROA, our target is to cross 1% on a steady state manner, which is what we are working towards.

Those are some of the few observations I wanted to share with you. If you have any questions, happy to answer.

Moderator: We will now begin the question-and-answer session. First question is from the line of from Mona Khetan from Dolat Capital. Please go ahead.

Mona Khetan:. My first question is on the slippages. You mentioned in the opening remarks about this corporate slippage in this quarter. But just wanted to understand how large is this quantum and could we expect slippages to normalize going forward?

Murali M. Natrajan: I think four accounts are in corporate. All these accounts are very old accounts. One account has been with us before I joined the bank and one account has been there since 2010. These accounts depend on repayment from quasi-government, government agencies, there are delays. In the meantime, they've had some challenges and these accounts although I would not say they were strong but they have been doing okay with us for the last many years. But some banks have taken that to NCLT, and therefore obviously, till the NCLT process is resolved, we can't get our payment. So, I don't expect this kind of slippages from corporate, at the same time we are working on resolution process and we are hopeful that in the coming few months we should get some recoveries on this.

Mona Khetan: What would be the quantum for all these accounts together?

Murali M. Natrajan: You can see that our corporate NPA has grown by about Rs.100 crores, so, that is the quantum.

Mona Khetan: The Rs.350 crores or so of slippage would sort of be the normalized number in the interim?

Murali M. Natrajan: We expect so… see, I would not read too much into gold loan slippages I explained that in the previous call also. Because, we give OD product and customers are expected by the regulation that came on November 14, 2021 in the OD product, including SME kind of OD product that every day they have to be servicing the previous 90-days. So, customers do slip into NPA, but again we recover all the overdues and bring them back. So, I would not read too much into slippages of gold loan. The rest of it I can say is looking like to us as a normalize kind of slippage.

Mona Khetan: Because of this kind of regulation and you are having a material gold book, is it fair to say that our slippage number as well as recovery numbers sort of going forward will remain elevated?

Murali M. Natrajan: Till such time, we are able to discipline majority of the customers to follow the rules completely. Also, we are looking at some alternate products for the customers in gold loan, whereby it can be like some kind of an installment/OD product, we haven't yet fully tested that with the customer acceptance, where they don't have to suffer this every day, 90-days. See, customers are taking gold loan as an emergency product. It is not necessarily that they deposit all their business receipts into that account, whereas in SME business and all, on regular basis some deposit is happening, therefore, they don't get too much affected by this every day, 90-days, even corporate loans get affected by that. So, I would expect elevated NPA especially in gold at least for some period of time.

Mona Khetan: My second question is, given that you primarily operate in the 30, 40 lakhs segment, how is the current inflation environment impacting the borrowers?

Murali M. Natrajan: I can only say two things. The demand for loan, when we are talking to our frontline for target and so on, I don't see any major resistance in terms of us asking them to perform at a higher level.

Secondly, the collection feedback seems to indicate that we are not having too much trouble trying to get some overdues and all from customers. Having said that, for customers if they miss one payment, it's not easy for them to make up two payments together because of the nature of their income and so on. So, I will say that, at the moment, I don't see too much challenge on that. However, we are passing on the MCLR increase and EBLR increase. And I do hope that it doesn't go too much beyond control because then sometimes the debt burden can be impacting some of the marginal customers.

Moderator: The next question is from the line of Rohan Mandora from Equirus Securities. Please go ahead.

Rohan Mandora: This was on slide # 26 where we are giving the trends on GNPA across last five quarters. So, the kind of improvement that we have seen in the mortgage GNPAs in last five quarters, we are not seeing similar trends in SME, MSME. So, just wanted to understand, is it because of the customer profile like there's a difference between the two or how should we read into the movement in the GNPA number in the two segments?

Murali M. Natrajan: SME, MSME, a lot of the portfolio is working capital and many of them are getting used to this every day, 90-days, keeping their accounts in order. So, the slippages there are mostly because of not being able to keep their interest serviced on every day, 90-day basis, which is the November 12th circular. Again, I'm seeing improvement in that, but we could do better, but I don't see any concern in the portfolio, post-COVID, things are stabilizing quite well, and even the recovery, upgrades are quite encouraging in SME as well.

Rohan Mandora: So, it would be fair to understand the new slippages happening and upgrades happening and it's not mostly a static book?

Murali M. Natrajan: No, no, there's a lot of movement, every month, there is some movement, and customers are coming and settling and there are customers who, after six months of having performed and their business doing very well, they are even requesting for enhancement. So, there's no problem with the portfolio I am saying. It is just the nature of how they're getting used to this. And let me also tell you, a lot of customers have come out of this COVID, they're performing well, their business is doing well. But yet, some of the old overdues and all, they're still catching up. If they don't catch up in a particular month or so, they slip into NPA. I've said this even in the previous call and all, it will take another maybe two quarters or so for this to stabilize.

Rohan Mandora: Just a follow up on this, in working capital loans, typically, he will need to service only the interest component. So, when you are saying that it's because of the daily recognition, daily tagging of the NPAs, we would have some turnover credit happening into the accounts. So, while for a mortgage, it's more of an EMI kind of a payment where the outgo is more lumpy in terms of servicing the loan. So, the difference wise, SME should ideally –

Murali M. Natrajan: In mortgage, if the customer has got, say, two installments to be paid and we collect one installment, he will still be non-NPA. But in the OD product, like I explained, read the November 12th circular, it says that on everyday basis, the previous 90-days, he should have serviced the interest. So, what happens then is if there is even a few days delay, suddenly you find that while he is a good customer, he has had regular payments, but he has missed that 90-day gap, then automatically he becomes an NPA. So, then now we have to service all three interest for him to become regular. That's the kind of regulation that we are dealing with. I'm not saying it's the wrong regulation, it is just that customers are getting used to that way of doing business.

Rohan Mandora: The cost of deposits have improved on a sequential basis. So, just wanted to understand what was the incremental cost for 2Q and how should we look at it for the second half?

Murali M. Natrajan: I think the cost of deposits will go up now, because if you look at the term deposit rate, there is a battle out there going on. The deposits are not that easy at the moment, it is tight. So, I do expect deposits to go up, I think the mix of CASA versus term have helped us. So, that is how the cost of deposits have come down. And some benefit also we'll get, because in a few days, as per our notice, we will repay x-amount of the tier-two, so that we will have some benefit also, but on the whole I think cost of deposit, cost of fund should go up.

Rohan Mandora: On incremental cost of deposits right now, how much more is it from the reported numbers for 2Q?

Murali M. Natrajan: I don't disclose all that number. You will have to wait for our next quarter result to see what that is.

Rohan Mandora: And lastly, on the corporate slippages. Historically, as I understand, what we had indicated is that on the corporate side, the loans that we give is typically less than one year tenor loans, and what you indicated is these are long relationships that we have had. So, was the deterioration in the -?

Murali M. Natrajan: We started doing short term kind of loans about four or five years ago. Before that customers do have OD loans, term loans, all that is there and they have been servicing, these customers also have been servicing the last 10-odd years. Unfortunately, they got into some trouble and then couple of banks have taken them to NCLT and therefore the whole process is taking time, and obviously, if there's no payment coming, we have to kind of classify that as NPA. Corporate loans, I've always explained for the last several years that there may be complete lull for a long time and suddenly one or two accounts do slip into NPA, that is how it has happened.

Moderator: The next question is from the line of Renish Bhuva from ICICI Securities. Please go ahead.

Renish Bhuva: Two questions. So, one was on the core fee income part, which has increased sharply to Rs.77 crores from Rs.65 crores in last four, five quarters. So, sir what is driving that, and one should assume this is the new sustainable range going forward?

Murali M. Natrajan: Processing fee, third party-income distribution, again, I've been guiding you guys that we are working with our frontline to improve our fee income, cross sell and so on. So, slowly we are seeing the impact of this in our P&L and we hope to improve it further.

Renish Bhuva: Secondly, on the credit cost guidance, when we look at the slippages even the ex-gold loan portfolio is still at more than 4%. And when we are guiding at sub-50 bps point of credit cost, what is the LGDs are you factoring?

Murali M. Natrajan: I've given you a general guidance on LGD terms. Secured portfolio LGDs are unlikely to cross, especially mortgages unlikely to cross 20%, 25%. That doesn't mean that is our LGD, but we don't see those kind of sacrifices to be made in mortgages, especially in small ticket loans and all. In many loans, we recover from penal charges to penal interest to everything else when we settle with the customers. On several of these customers, you see, there are upgrades and recovery. So, I'm guiding this based on what we see as our portfolio. And we believe that our credit cost which I have indicated in one of the things should be in the range of 50 basis points. So, obviously, we are experiencing lower credit cost. But I believe that our business model seems to indicate to me that 50 basis points is the model that we will be moving towards.

Moderator: The next question is from the line of Bunty Chawla from IDBI Capital Markets and Securities. Please go ahead.

Bunty Chawla: Continuing with the gross NPA movement on the slide 26, historically, what we have observed that we generally don't believe in write-offs or sacrifices kind of a thing, and run rate also was approximately Rs.2-3 crores per quarter, but this quarter, it's slightly higher, Rs.41 crores approximately. So, any strategy change or any outlook change on that part? And also, if you can share this Rs.41 crores belonging to any specific segment or something like that?

Murali M. Natrajan: The Rs.41 crores belongs to various products, and I do believe the average ticket size on that would not be more than maybe 20, 25 lakhs, which is similar, fully provided. So, there is no strategy or anything like that. So, we just look at some of these loans, we review it, and we see what is the timeframe that is required for recoverability, and then based on our discussions with the collections unit and all, we take a call, maybe this needs to be written off. So, we don't pursue write-off as a way to reduce our NPA, you know that and so that's what it is. So, this quarter, we have reviewed it and figured out that about Rs.41 crores, that is what we have done. So, there is no big strategy behind this actually.

Bunty Chawla: Secondly, Sir, if you see, there has been a still high amount of run rate on the operating expenses continuously happening, though we have earlier said still we are focusing on the branch expansion and all those things. But when is the trigger that employee expense or total operating expenses will have a sustainable growth and higher operating leverage will kick in for us with respect to cost-to-income ratio?

Murali M. Natrajan: We are adding frontline people in mortgages, in SME, in KCC, in tractors, in gold loans in branches, in deposits, all these areas we are adding these people. We have lost some time last year and so on because of COVID. We obviously cannot catch up on the entire balance sheet, but we're saying okay, there is an opportunity, there is a demand in the market, we are seeing very good performance on our credit provisions and so on, we are seeing a decent increase in our NII, fee income core is doing well. So, we want to make sure that we have adequate capacity for us to be able to double the balance sheet between three and four years and continue the same momentum. Like I said, between 2010 to 2020, on a CAGR basis, every year we have grown our loan book by 22%. So, we have the ability, we have the product, we have the technology, we have the market, we understand the segment, all that. So, next year, I don't expect year-on-year expense growth to be at this kind of level because we would have already reached a platform of capacity, that would help us to build our balance sheet at that level.

Bunty Chawla: Lastly, on the margin per se, if we see, still we have got the benefit of decline in the cost of funds and cost of deposits during this year and we expect yield on advances which has increased because of the repricing, but still there should be some more repricing happening in the next two quarters. But on the net interest margin, still we are guiding, there should be a 3.65 to 3.75, already we have touched 3.9 for this quarter. So, how one should see for next two quarters net interest margin movement?

Murali M. Natrajan: This is the most difficult question for me to answer, because there are so many moving parts of this, from meeting the agri target to deposit rates to refinance that we get from NHB, the rate moves on that, to pricing on our CASA to the product mix, to NPA movement, there are so many pieces. Our business model is we are quite happy with 365, 375 kind of range on NIM with 50-odd basis points on credit cost. What is work-in progress is that we are building capacity for stepping up the growth which we are demonstrating to you, and that costs start to come up, that is one. And the fee income, also we are demonstrating that it is going up. I wish exactly on a linear manner, like what we do in spreadsheet, it keeps going up. Sometimes, it is not the way that business works. Like, for example, we got some hits this quarter on corporate. Had it not happened, our NPA would have been even far better than this. But we still were able to manage to get sufficient recovery and upgrades and our restructured book is also performing quite well. So, I would say our business model is on the same page. Let me assure you, we are not working towards reducing the margin towards 370 basis points.

Moderator: The next question is from the line of Krishnan ASV from HDFC Securities. Please go ahead.

Krishnan ASV: You just alluded in your opening remarks at some stage you will be more responsible, all lenders, I'm assuming will have to exercise some responsibility in how much more to exercise the pricing power on the asset side? This is something I think I have been trying to kind of get grapple with across the system. Does EBLR allow you that kind of elbow room or does it need a separate dialogue with the RBI or is it usually just in the nature of business as usual, that whenever customers come up for annual resets, etc., this is something at the bank's discretion that you could move the spread around? When do you see that stage ideally coming through? Would it be, say 50 basis points from here if the repo was to go another 50 basis points or does the consumer seem willing to pay even now?

Murali M. Natrajan: Neither EBLR nor MCLR gives you any way not to pass on the benefit or the increase. It's a very straightforward formula-driven method. It is audited by statutory auditors, and it is also audited on a yearly basis by the regulator. So, absolutely, you cannot make any of the thing. I've seen some banks reduce MCLR or increase MCLR in the multiples of five and stuff like that. But if you look at our MCLR, you'll see that it is like 14 basis points and 27 basis points, because we do it absolutely exactly whatever comes, we are either passing it on or reducing as the case may be. However, based on the segmentation of the customers, we do have the right to reduce our credit risk premium or increase the credit risk premium in case we find it is a risky customer or the customer has got good track record and so on. That's the one flexibility we have. It can't be whimsical, it has to have a policy, it has to have a process, only then we can do that. So, I was referring to those kinds of customers rather than affect them by this because they are good customers, in a structured manner, not giving some benefit of their good performance. The second thing is there are marginal customers for them further increasing the rate might actually affect them, in which case, we'll have to segment that and look at how we handle that in collections so that we don't give them all the edge or give them some kind of education such that they don't push themselves into a corner. That is basically what I was referring to. And these are all stuff that we do as a regular basis.

Krishnan ASV: Just from an EBLR transmission perspective, could you just advise on how much more room there given the customer profile that we cater to, how much more –

Murali M. Natrajan: I don't have the answer, but we have customers who are all in the high score, our cutoff is 700. So, we don't give loans to low score customer. So, therefore, if at all there is something, it will be a very small portion of our portfolio.

Krishnan ASV: On the deposits side, it's fairly evident that there is a scramble for deposits. In your pockets, you believe that DCB is disproportionately lower given its own known market fair, are there pools of deposits where you're disproportionately lower where you've still not made serious inroads?

Murali M. Natrajan: I'm not completely understanding the question. In the retail segment?

Krishnan ASV: Or in the institutional segment, you also begin to participate with the sovereign at all?

Murali M. Natrajan: No-no, institutional deposits have very different treatment in LCR. All banks have to pursue only retail deposits, because if you pursue too much of institutional deposits, then you will end up in having a LCR problem unless of course you are giving a non-callable kind of a deposit. So, we are very happy with our participation in all these stuff. However, our core effort and strategy is to keep on pursuing retail deposits. And in retail deposits also, you can't be a hero. Supposing, some of the competitive banks are at 7.25, you can't expect to get pricing at 6.9, it doesn't work like that, because the market is very competitive. So, you have to be at the market at that rate, otherwise, you don't stand a chance to get that deposit. So, I will say that, generally, the deposit situation is a bit tight; however, so far we are doing quite okay.

Moderator: The next question is from the line of Gaurav Jani from Prabhudas Lilladher. Please go ahead.

Gaurav Jani: I think we have changed our disclosures. So, this was relating to deposits. So, Q4 FY'22, the wholesale term number or the share was about 9% Could you quantify that for Q1, Q2 percentage or absolute either? The data was in the presentation. So, it was taken from there.

Murali M. Natrajan: It maybe in the same range, 10% or 11% like that, that's all

Gaurav Jani: No, just wanted to understand as to how has been the movement of retail TDs over the last quarter?

Murali M. Natrajan: Retail TDs movement is okay, but like I mentioned to you that the deposit market is somewhat tight and competitive. Therefore, we have to keep reviewing it almost on a weekly twice the basis to make sure that we are right out there to get the momentum on the deposits going including our RNP CASA. RNP CASA is not that problematic. I think it is moving very well for us. But given our ambition for loan growth, we have to be out there to make sure that we provide that liquidity. So, so far, we have not faced too much of a challenge, but quarter-on-quarter, there may be some increase in wholesale deposits, because we have to balance these things, because maybe momentum building on retail deposits maybe taking some 45-days, 60-days extra, in the meantime, you take a wholesale deposit, non-callable deposit, make up for the liquidity and then build up your retail deposit. So, these things we have been doing in a continuous manner.

Gaurav Jani: So, for the quarter, would you have seen a retail TD growth of about 5% quarter-on-quarter?

Murali M. Natrajan: I don't have that number.

Gaurav Jani: Taking the discussion on yields forward, I think because obviously of our product profile, the yield increase over the last few quarters on a quarterly basis has been rather slow as compared to the competition. So, should we expect slower, at least the numbers indicate that, but so over the second half, should we see yields increasing at a faster pace?

Murali M. Natrajan: We are focused on NIM. Our target NIM like I said is 365, 370 basis points. We have a mix of products. Within mortgage itself, we have some five, six different products, then we have KCC, tractors, then gold loans, there are different pricing for different ticket prices or segment, then SME we have. So, it's very hard for me to exactly say how this will be. We monitor our yields and NIM on a weekly basis to see how we are heading. And we are quite confident that we'll be able to maintain the NIMs of between 365 to 375 points.

Gaurav Jani: So, coming to asset quality bit, if I had to look at slide #27, you have interestingly mentioned that the restructured pool by March '23 would come down from 1,900-odd crores to about Rs.400 crores. So, that's a huge –

Murali M. Natrajan: Where are you reading this Rs.1,900 crores? Did I say that Rs.1,800 crores or Rs.1,900 crores is under moratorium? That is not what we have said. We have said that the moratorium business of Rs.400 crores, not all our restructured is moratorium.

Gaurav Jani: So, coming to the credit cost bit, sir, you mentioned in your opening comments that we're targeting 50 basis points. So, would this be for '23 and are you guiding that for the coming years, and what will give you the confidence of maintaining the 50 basis points?

Murali M. Natrajan: On a steady state basis, we believe the product mix that we have, the segments that we are operating in, the credit structure, collection structure, all that put together, should give us NIM of about 365 to 375 basis points and a composite credit cost of 50 basis points. We are not big on corporates. Even if you're not big in corporate, you can get here and there hit by some corporate NPAs. So, I don't count any noise created by corporate here and there once in a while, other than that the basic portfolio which is a retail and SME portfolio, we believe should operate in that range.

Moderator: The next question is from the line of Bajrang Bafna from Sunidhi Securities & Finance Limited. Please go ahead.

Bajrang Bafna: My first question is understanding on the restructured book, if I recall the last presentation where we guided that the restructured book under moratorium will come down below 700 and now we are guiding that by March '23 it will be 400. So, can you bifurcate the book between moratorium and non-moratorium under the restructured category, and how that overall movement will be?

Murali M. Natrajan: I've said that by March, we will be at 400. Last time I said by September it will be 700. So, the moratorium is every year month. So, from 700, it's moved down to 400 on a monthly basis, that is as simple as that. The rest of it is always bill book.

Bajrang Bafna: So, how do we see the movement of overall restructured book by March '23?

Murali M. Natrajan: The restructured book will remain as restructured. It's a standard restructure. There is no provision in RBI to say that it is not a restructured anymore. Unless the customer comes and pays off the full money or it goes to NPA, anyway will stay as a restructured book. Even there, we are seeing that a lot of customers are closing their account straight at the restructure research stage itself and many of the customers after having come into billing and after we have kind of done some collections, some of them are moving into NPAs as well. So, the slippages include even the NPAs that may have slipped after coming into billing. The restructured book will be termed as restructured till such time it becomes zero.

Bajrang Bafna: Once it is restructured, it will continue as it is till the time the customer fully pays it off?

Murali M. Natrajan: Yes.

Bajrang Bafna: My second question pertains to the growth capital. How are you seeing the growth that you are saying 20%, 25% kind of run rate for next couple of years, when can we expect that threshold of capital adequacy will be achieved at which we will look for fund raising, so, can you guide on that, it will be really helpful?

Murali M. Natrajan: Our projection indicates that at about 15%, 16% growth rate, we will be self-funded, because for Rs.100 of loan, we are only consuming about Rs.60 as the risk weighted asset. It's a very capital-efficient model. Unless some weightages are changed by regulation or we change some product mix which we are not planning to do, at 15%, 16%, we are sufficient. However, our aim is to grow at a much faster pace. So, at least for a year, I don't see… and you know that the half year profit is not included in the tier-one computation, it will be included only at the year-end after the audit is completed, right. So, therefore, we believe that at least for a year from now, we don't need to raise capital.

Bajrang Bafna: So, not in FY'24, maybe somewhere in FY'25 we can think it off?

Murali M. Natrajan: No-no, I said a year from now.

Bajrang Bafna: So, September '23?

Murali M. Natrajan: Yes, I mean, I'm just saying that at least for a year from now. Read all my statement, a) 15%, 16%, I don't need to raise capital; second, our aim is to grow much faster like doubling the balance sheet between three to four years. Current year profit is not included in the computation. All put together, then the markets also has to be favorable for us to raise the capital. At the moment, we are pretty strong on capital adequacy. So, I don't see any immediate reason for us to raise capital.

Bajrang Bafna: The last question pertains to, what percentage of our total loan book is floating right now?

Murali M. Natrajan: We don't have that information here. But majority of our book is either linked to MCLR or to EBLR. In the last few years, it is linked to EBLR, before that it is linked to MCLR. And we haven't seen any problem in passing on the increases to our customers.

Bajrang Bafna: So, mostly the book is floating, so we will not deal under -?

Murali M. Natrajan: Yes.

Moderator: The next question is from the line of Anil Tulsiram from ContrarianValueEdge. Please go ahead.

Anil Tulsiram: My first question is on competition. So, from next year, the account aggregator system will I think become operative. And in addition to that, we already co-lending. So, just want to know, whether these three coming together will put any impact on our NIMs and competition will increase much more than in the past?

Murali M. Natrajan: It's a very difficult topic to engage at this point in time. Even we haven't fully understood the implications of how this account aggregator will pan out and what would be the impact and how many would participate. I think the customers all have to say yes to it, right, each of them. So, there's a lot of open items in this. So, I don't believe that we can bottom out our discussion here. So, you have to give us some more time to understand this.

Anil Tulsiram: Second last question is do we lend on the basis of informal income, or all our loans are based on the formal documented income?

Murali M. Natrajan: Let's just take example of only mortgages, there are multiple products we have in mortgages. At a high end, including income tax returns to P&L, we take including bank statement, at a low end, I'm just giving an example, and this is my favorite example, so I'm repeating this example would be wife is doing tuition, husband is, let's say, some kind of a motor mechanic or something and son is doing some small jobs somewhere, we'll be able to put together all their income and come out with a debt burden with which we can actually fund them a home loan. And part of it will be informal, most of it will be formal, because we will go through bank statement and other whatever information is available before putting together. It is very hard to just use only informal income and get somebody's paying capacity, that's very, very hard, I mean, I don't think we have any such product. So, it'd be hybrid at the low end, but fully documented at the high end.

Moderator: The next question is from the line of Sharaj Singh from Laburnum Capital. Please go ahead.

Sharaj Singh: AIB book, we have seen good disbursement. So, what has led to this? And also the incremental disbursements are not actually reflecting in the loan book growth in absolute terms.

Murali M. Natrajan: Which book you are saying?

Sharaj Singh: The Agri Inclusive Book, (AIB)?

Murali M. Natrajan: So, what is your question, that it is not reflected in what?

Sharaj Singh: The loan book growth in absolute terms. So, how much of this is actually repayment and how much -?

Murali M. Natrajan: AIB must have grown at least 18%, 19? So, I'm not sure where you're looking at on this.

Sharaj Singh: If we look at the quarterly number, so how much of this is actually normal prepayments and how much of this would be takeovers or -?

Murali M. Natrajan: In AIB we have number of products. AIB has got tractors, AIB has got KCC, AIB also have retail products like mortgages, SME, and AIB has microfinance through BC and AIB also has term loans to MFI entity. So, if one or two MFI entities have repaid their loan or something like that, then it maybe reflecting in this thing, but the core retail business of AIB which is the KCC, tractor, mortgages, BC, that is doing quite well for us on a steady state business.

Sharaj Singh: On the mortgage side, what is the normalized BT out and BT in also?

Murali M. Natrajan: There is nothing unusual that we have seen in the last 12 months. Approximately 20% of our book would be from other financiers, because customer is trying to arbitrage on his interest rate. As the COVID started easing up, we did see some jump in increase in what you call as BT out. But when interest rates are increasing, you don't see too much of jump in BT.

Sharaj Singh: Given the normalized rate, I mean, normalized what would we see -?

Murali M. Natrajan: We don't present that information.

Sharaj Singh: Regarding the fees income, do we have a target where we'd like to take this as a percent of our asset?

Murali M. Natrajan: We want to achieve 110 basis points. That's our target. We probably are about 90 basis points at this point in time.

Sharaj Singh: On the restructured book, I think peaked around Rs.2,150 crores and Rs.700 crores is still in moratorium as on date. So, the Rs.1,300 crores, that has come out of a moratorium?

Murali M. Natrajan: Rs.700 crores is not on moratorium. Rs.700 crores was in September, so October have already come in, in November something will come in, so every month something will fall off the moratorium.

Sharaj Singh: Of the Rs.1,300 crores in September, how much of the moratorium book came out in Q2 FY'23?

Murali M. Natrajan: Please refer to page #27. By March, only Rs.400 crores of moratorium will be left. So, you can do the math as to how much is coming out because that is all the information we can give you at this stage.

Sharaj Singh: I was actually asking, 50% is already out of moratorium as on September 30. What percent came out in Q2 out of moratorium?

Murali M. Natrajan: I don't have that number. All I can say is our collection efficiency that we are showing you includes those who have come out of moratorium and paid. So, we have two collection efficiency data; one is on zero bucket, another is on including delinquent and restructured, you can see that business loans are at 96.7, home loan is at 98.1, so that should give you comfort. I have repeated this many times, we have not restructured any unsecured loans. So, when a customer comes out of moratorium, it takes about two, three months for them to come into the rhythm of repayment.

After that, our collection people are able to get them back on track. Those who don't get back on track, slips into NPA. That is already reflected in our slippages.

Moderator: The next question is from the line of Darpin Shah from Haitong India. Please go ahead.

Darpin Shah: So, my question again was on yield. So, we see yield has gone by around 15, 20 basis points on a sequential basis. So, just wanted to understand how much card rate increase which we must have done already on the loan side and what will be the reset which is happening?

Murali M. Natrajan: I didn't understand your question. What is the question?

Darpin Shah: Our entire book is largely floating in nature, whether linked to MCLR or EBLR. How much card rate increases we have already taken say from April till now and what will be the reset period because this increase of 15, 20 basis points sequentially looks much lower for a floating rate book actually. So, that is what I was trying to understand.

Murali M. Natrajan: See, the MCLR is passed on four times a year, correct. But it is reviewed every month and then as per sanctioned term, they are passed on in a particular day, November, then February, then May, and then August. These are the four months in which it is passed on. So, it has a little bit of lag in terms of passing on that. Whatever book was priced in EBLR, that has already been passed on. EBLR has come in only a few years ago, so not all our book is on EBLR, so you won't see the entire thing impact, and I think 50 basis points needs to be passed on next month, right. So, you will see some impact on that.

Darpin Shah: So, in that case, we can expect that at least the third quarter, fourth quarter margins tilt to remain at these levels and then by FY'24 it might be in the range, which you have always been talking about?

Murali M. Natrajan: We are looking at a margin of 365 to 375 basis points. It is very hard to explain every moving part in that. All of a sudden, for example, if there is a huge competition in market on deposits, given our growth ambition, we can't stop there. So, we'll have to look at saying, okay, why don't we do some differentiating pricing in liquidity, and it may have some impact on margin in that part, but we'll have to change our product mix profile to make sure that we come back to margin. These are nuances and adjustments we keep doing on a monthly basis. So, it's very hard for me to explain mathematically exactly how this is going to flow especially with so much of mix of products.

Darpin Shah: Lastly, a data question, if I can get breakup of the provisions?

Murali M. Natrajan: Breakup of the provisions is there on page #30 I think no.

Darpin Shah: For the quarter?

Satish Gundewar: You want to break up on that Rs.31 crores number, right? The floating provision is about Rs.4 crores, standard restructuring provision is a reversal of Rs.11 crores, the regular standard asset provision is Rs.7 crores, and the NPA provision is Rs.31 crores.

Darpin Shah: Can I get for 1Q as well if it is available?

Murali M. Natrajan: I didn't get you.

Darpin Shah: Can I get the same number for previous quarter, that is Q1 FY'23 if it is available?

Murali M. Natrajan: We don't have it readily, but we can give it to you later.

Moderator: The next question is from the line of Pallavi Deshpande, individual investor. Please go ahead.

Pallavi Deshpande: Just wanted to ask, what would be our guidance on the slippages part and we've seen a slight uptick from March, what would be the reason for that?

Murali M. Natrajan: On the slippages, given that we are coming out of COVID, given that we have a self-employed book, given that a lot of the customers are improving, stabilizing, so we do have a situation where customer who has got upgraded let's say last year December may have slipped and then again getting upgrade, because they're all stabilizing their business. So, I do expect similar situation, but I don't expect every quarter some corporate slippages to be like this, because it's more like once in a while kind of stuff. Gold loan slippages still like I explained, would continue to be high because of the OD product that we are doing and the recoveries and upgrades also would be high. So, I would say that it may remain like this for at least another two quarters before kind of tapering off.

Pallavi Deshpande: In terms of the steady state which is ex-gold loans, what was the state, because you've given us a credit cost guidance?

Murali M. Natrajan: Our credit cost is targeted at 50 basis points. So, that has a composite of slippages, recovery, our portfolio quality, our loss given default, everything is built into that, and if you go back till 2019-20, you will find that we have operated at the level. Also, if you see, we also have a target of at least keeping our operating profit three to four times the provision. I think prior to COVID, that is the kind of safety margin we had, and I think we are pretty much back to that same level. So, that is what I can guide you on. Exact slippage ratio at all, prior to COVID, we were operating at about 2.5% or something like that. So, our intention is to go towards that, but I think we have some time before we reach there.

Pallavi Deshpande: Lastly, on the net interest yield improvement that you've seen, which segment would it be driving -- would it be gold loan that has seen the maximum improvement from March to September if I am comparing?

Murali M. Natrajan: So, every segment is highly competitive. Even gold loan is very competitive. Many of the banks have not even increased their rate despite EBLR increase and cost of fund increase on gold loans. And small ticket gold loans are operationally intensive. So, it may be giving you a good yield, but the cost of operation is high on small ticket gold loans. So, there are these complications and nuances. So, I would say the mix of products that we are operating, we should be able to maintain NIMs at about 365 to 375 basis points.

Pallavi Deshpande: What is the average size on our gold loans?

Murali M. Natrajan: About two lakhs. That is our average ticket size. Actually, if we go down to 50,000, 60,000 kind of level, we can come on higher interest rate, but it becomes operationally intensive. Also, those customers demand faster turnaround, which I would put my hand to heart and say that, we have not been able to crack the model followed by some of the gold loan NBFCs. They do it very efficiently. So, we are still a little away from that kind of ability to service those customers.

Pallavi Deshpande: In terms of the MSME mix, how much of that would be export-focused and how much would be domestic?

Murali M. Natrajan: Mostly ours is domestic because we are all small ticket size at 30 lakhs, 35 lakhs kind of range. Mostly, wholesale traders, small manufacturers, that kind of thing. So, our export thing would be quite small, maybe not even 5% to 7%.

Moderator: The next question is from the line of Anand Venugopal from BMSPL. Please go ahead.

Anand Venugopal: Sorry, I joined a bit late. Pardon me if this question is already answered. So, I was just having a basic question like slippages still stay elevated, but recoveries and upgrades save the day for us. So, could you provide some color on what accounts are slipping and what accounts are getting recovered or upgraded?

Murali M. Natrajan: Upgrades and recoveries are not an accident, it requires effort, and it also is reflective of the portfolio quality. So, it is not some luck that we have had on upgrades and recovery. So, I would like to correct you on that right away. So, it's a part of the portfolio quality and the resilience of the portfolio that is indicated, and we have almost 1,000 in-house collection team who work with these customers, these are all secured portfolio, and we are constantly in touch with these customers to make sure that they are upgraded. The upgrades are higher than recoveries, that tells you that we want to retain the as much of these customers as possible, because an upgraded customer is good business for us for future earnings as well. So, I expect slippages to be pretty much in the same kind of level for another two, maybe max three quarters before it starts to ease off.

Moderator: The next question is from the line of Sharaj Singh from Laburnum Capital. Please go ahead.

Sharaj Singh: My question was on the branch expansion we're looking to do. What do we target over the next two years in terms of the branch network? Is it mainly in the tier-two, three towns or how do we look at it?

Murali M. Natrajan: So, the bulk of the deposit still in my opinion comes in the top 60, 80 locations in India. So, to some extent, we have to open branches in the top 60, 80 locations. As you know, if you open 100 branches, 25 of them have to be opened in unbanked location. That's a very tough business to break even in two, two and a half years' time and sometimes it takes even four years in these unbanked locations. Our intention is to grow our branch network between 25 to 35 branches, and I think we are on track this year also on that.

Sharaj Singh: So, basically we can expect a branch expansion increase?

Murali M. Natrajan: Sorry?

Sharaj Singh: We can see a higher ramp up in H2. I think you opened 10 branches in H1.

Murali M. Natrajan: Generally, most of the branches we open between Q3 and Q4, and then they start to perform by first quarter. Last year, whatever we opened, is starting to give us benefits.

Sharaj Singh: On the yield side, have you already taken some compromise on the spreads that we have in terms of passing on the cost to our borrowers?

Murali M. Natrajan: What have we done -- passing on the increases?

Sharaj Singh: Have we already taken some compromise on the spreads?

Murali M. Natrajan: Right now, whatever increases, that is getting passed on to the customers. There is a separate analytics team which looks at good quality customers and has programs from a both retention point of view as well as from growth point of view to pass on some benefits purely on a credit performance basis.

Moderator: As there are no further questions, I now hand the conference over to management for closing comments.

Murali M. Natrajan: Thank you very much for attending this call. I know this is Saturday, and it's already 7:30, but I appreciate your patience, and appreciate your participation, and look forward to talking to you next quarter.

Moderator: On behalf of DCB Bank Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.