“The Federal Bank Ltd. Q2 FY22 Earnings Conference Call”

October 22, 2021

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Moderator: Ladies and gentlemen, good day, and welcome to the Q2 FY'22 Earnings Conference Call of the Federal Bank 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 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. Anand Chugh, Head, Investor Relations. Thank you and over to you, sir.

Anand Chugh: Thank you so much and good afternoon everyone. Hope you would have seen the numbers and you would have seen that this quarter has been a pretty solid quarter for the bank.

Before I kind of hand it over to Shyam for his opening remarks, I would like to kind of bring to your attention some accounting change that has been brought in because of in compliance of RBI Circular dated 30th August 2021. Couple of changes which are important for all of us to note: One is that recovery from written off asset which earlier used to be accounted under other income, now has to be netted off against the provision for NPL. Also, any provision or depreciation for standard investments which was earlier accounted under provision and contingency is now netted off against other income. So, these are two changes; number one, there is no P&L impact or the bottom line impact of any of these provisions. But there are some line items have moved from A to B and B to A.

And second is, just wanted to kind of ensure that all of us are on the same page, we have adjusted the past numbers so as to give you a comparison of quarterly numbers on like-to-like basis. So, I'm sure all of you would have taken note of that.

And with these opening remarks, I would possibly request Shyam to kind of give his commentary on the quarter gone by and then probably we will proceed with Q&A. Over to you, Shyam.

Shyam Srinivasan: Thank you, Anand and good afternoon, everybody. Like Anand mentioned, we do think that we had a good quarter given all the challenges in the environment. We are seeing a good traction on the many initiatives the bank has been putting in for long periods of time. And we've literally tried to build a bank brick-by-brick, and it's good to see some of them coming to its rightful place.

Most important being the asset quality of the bank, in particular this quarter was a great tribute to the efforts of the bank, we did see. slippages very modest, but recovery upgrade way above even slippages considering that we did have slightly better slippages in the last quarter, we saw them come back quite well. So, as a consequence, credit costs for the quarter was flatteringly remarkable with literally no credit costs for the quarter which would be a very happy place if we were to repeat it all the time overall all over again. Interest income grew well; NII was at about Rs.1,479 crores, our all-time high. Noteworthy was a very strong traction on fee income, non-treasury, core fee income grew very smartly and CASA continues to be our sort of strong bed and we saw that go up to 36.16% in this quarter. And our liability franchise continues to be one of the most coveted, I would say, with large part of it being absolutely granular in retail.

So, the quarter that went by, we do see the credit pick up in many areas, and most of them are seeing traction as we go into the second half of this financial year. Many areas of retail have started seeing good momentum. Happy for us that business banking and commercial banking have also started seeing growth. And we saw annualized for the quarter, roughly 12%, 13% growth, which is a good sign. And that's not by diluting credit standards, but by increasing our coverage penetration and sort of competitiveness of our offerings.

So, in short, the quarter did see good progress on many counts, the numbers are there for you to see; it did see 50% growth over last year same quarter net profit and sequentially 25%. But I think those are less relevant. From a long-term point of view, our commitment to get to that sort of minimal requirement of 1% RoA and keep heading north from there is well on course. This quarter was 0.92 and we believe that as mentioned earlier, the financial year '22 we will see exit at that 1% plus RoA and then keep moving along that line as I pointed out in our earlier interaction. We believe that 1.2, 1.25 over the next two financial years is what we will seek to do and there are lots of initiatives that we have put in place to make sure that those come alive.

There is one challenge which is visible for everybody is people related expenses have shot up, not because we have hired more or paid ourselves more, but this has a longstanding bearing on the pension cost and the recent announcement by government and the IBA negotiation for family pension, and the increase in annuity costs, the DA going up. These have unfortunately, skewed the pitch. But I've decided that there's no point being either defensive about it or worrying too much about it. What we can't control, we will just work through other lines and ensure that our desired outcome of 1% plus ROA is well on course, and not get distracted by these, which seem to now something that we have to content with.

That said, there are lots of initiatives. Many of you have seen an internship program we've launched, which is the first of its kind, and we believe over the next two years that would give us both sales momentum and keep our front end origination employee costs much lower because our sales person who comes in through this program, gets intern and also can do a sales job. So, we think that's one of the initiatives we've taken to cover off some of these costs which is a longer term problem in addition to our great and well run Fed Serv proposition which is helping us take away a lot of the costs.

The last part and important point, which you may have all observed, we have a fetish and a feverish pitch on digital and fintech. I have personally spent disproportionate time and Shalini as an Executive Director, probably spending a large part of our time on getting this going. We've created exclusive teams that are focused on this. At this point in time, there's a cost element to it. But we are willing to take that cost because we believe that in the long run, this is going to be a Federal Bank, completely differentiating from many other banks. Six years back I said, our strategy is digital at the fore, human at the core and branch like distribution heavy. We've added branches, we've added RMs, we've put in a digital stack that is helping us fintech players to covet it as their partner bank. You may have seen we've got very good partnerships. In the last three or four months, we've seen what three, four lakh accounts being opened. This will graduate, it's not going to be an instant win where they will all start building balances and become the huge portfolios. But we believe that done well, this is going to be a game changer for Federal Bank in terms of being the truly one bank, which has a hybrid model of digital and conventional banking practices coexisting. My words may seem like a flighty statement now, but I think we have the conviction that this over a period of time will be something that Federal Bank will be truly differentiated. If you pull any of the partners in the market, they will clearly believe that our engagement model is something that they respect a lot and the technology capability. And this is something that we are investing into.

So, my headline opening messages, performance has been pretty reassuring. We believe that our promise to be that 1% ROA bank is well on course. We are not taking our eyes off all the deliverables. The efforts have been quite determined. The growth in NII and consequently NIM is visible. Core fee income is tracking well. Generally, business momentum is beginning to pick up.

Credit quality in Q2 was remarkable. Sorry, I forgot to mention, we did restructure about 1,000-odd crores of assets which we will come to when I'm sure there'll be question and answers around that. And we have made sufficient provisions for that also anticipating what kind of slippages may happen over the next two to three years on that book and build up. I said about five quarters back that our PCR will never come below 65. And we're confident that whatever happens, that number will be honored. And we are tracking quite well to make sure that not just this quarter, but in periods ahead, those numbers will be contained.

So, with that, let me just hand it over to the operator. You may open up for questions. Thank you very much.

Moderator: We will now begin the question-and-answer session.

Shyam Srinivasan: I forgot to mention the entire senior team is there. I don't know if Anand mentioned it. So, they will be able to answer pointed questions in specific areas.

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

Renish Bhuva: Just first question on the margin side, which is currently at 3.2%. Now, in context with the lowest ever cost of funds and broadly, loan mix is also at a desired level, so how do you see margin sort of behaving over the next couple of years and also, if, let's say, interest rate cycle has to reverse, maybe within six, nine months, then how we're positioned to sort of get the benefit or is there to increase in the margins?

Shyam Srinivasan: I have always said, Renish, between business mix, the growth in our low cost deposits, and the reversal of interest income because of lower or higher slippages, the combined makes the margin looks good or bad. And we always guided at 3.20, 3.25 is where we will be, we are at about 3.20 now. I think the business mix and hopefully, more modest slippages in passage of time will cover up for whatever interest rate costs that may go up in periods of time. But it's obvious if you look at our ALM profile, we may be amongst the best players when the interest rate cycle turns up and we are a largely retail franchise, right? So, I'm not that alarmed by interest rate increase by itself. I also think sanity will come in the pricing structure for credit, because at some point is almost sometimes sounds insane. I see some kind of order will come in the market in the quarters ahead.

Renish Bhuva: Just a follow up on this. So, let's say whatever new products we have launched over the last three to six months maybe in terms of MFI or credit card, or over the next six months, we're going to scale the CV book, So, I mean, directionally, the margin should settle at 3.5, 3.4 or do you expect this is too early to comment on it?

Shyam Srinivasan: I have never commented on that higher number. I've always said 3.20, 3.25. So, we will work on it. We can only give you the mix of the business, the kind of credit quality and almost derivative you can derive the number but at this point in time, my site is 3.25 max 3.30. But I'm not commenting beyond that.

Renish Bhuva: Other OPEX went up by 20% sequentially to now in absolute terms touching 48.7 crores versus let's say 35-40 crores or four, five quarters back. And since we have not added any branches, I'm assuming these incremental 10, 15 crores are largely towards building the technology platform and all those things. So, going ahead do you see this OPEX stable at current level or we still have to invest more maybe over next couple of quarters, I mean, how one should read this OPEX line item?

Shyam Srinivasan: The OPEX line in parts for example, significant part of the increase is the variable one which is linked to say the sourcing cost which we pay to our DSA or Fedfina or what have been our acquiring business costs, what we pay for rupeek for our gold loans. So, to that extent, this is a variable. If volume comes, business comes, this cost comes. I'm not too worried about that. I'm not in great control of is the pensioning and the annuity costs, which we're working alternatives. I don't have a direct control over that. We are in fact working with the government to remove that rule 89 which allows us to self-ensure so to say, I don't have to buy annuity. But those are little long shot. Our OPEX by itself non people, is not something that we are nervous about, it's very much in control. We don't have any extravagant expenses, all our expenses are volume-related.

Moderator: The next question is from the line of Mona Khetan from Dolat Capital. Please go ahead.

Mona Khetan: I have two questions. Firstly, on the business banking and commercial banking book, we have seen a very good growth on a sequential basis; 7% to 8% each. So, what are the incremental yields in this segment, and any commentary around the demand scenario and the customer acquisition strategy will help? And my second question is around your remittance market share, which has increased to over 20% from 17.5% one or two years back. So, what is helping this rise, some color around that.

Shyam Srinivasan: Thanks, Mona. I think glad you pointed out the remittances. It was in my opening remarks. I miss mentioning it. Yes, this quarter comes with a one month lag. So, actually, it's the one quarter lag. We have literally become a fifth of India's remittances. It's been a focus for the bank now for many years. And from about 6% share now at close to 20% share over the last seven, eight years is something that we are greatly proud of. It is, like I said at the top of the call, brick-by-brick, we have field presence, we have technology capability, we have very good partnerships, good offerings, and speed to market. And every time some competitor blinks, we're there to take that share. It's a focus of the bank and we believe that we will do everything to protect that. So, I'm happy that the 17 has become 20. We have some internal ambitious targets. But yes, this 20 would be our sort of what we will try to preserve. On your part on growth in business banking, and commercial banking, we've always said that these are incremental growth opportunities for the bank. So, it's an area that we are quite strong at. And after we verticalized more sharply, there are RMs covering each of these businesses and branches are helping our business banking flourish, and the RMs are focusing on the commercial banking. So, there is sharp line of sight. I think opportunity exists; as India comes back and growth comes back, we will see a bigger share of our pick up on that. Yields, I'm not saying that these are disproportionately higher and certainly much better than corporate banking. And it's more granular. So, we are more excited about this business. The commercial banking is mid-8 to 9.5 and business banking is a touch higher 9.5 to 10, 10.5.

Moderator: The next question is from the line of Gaurav Kochar from Mirae Asset. Please go ahead.

Gaurav Kochar: My first question is with regards to the liquidity on the balance sheet. If I add the cash and call money, it's roughly 10.6% of assets. It used to be 5%, 6% earlier. I also see at the same time borrowings up 15% sequentially despite we did a capital raise allocation to IFC that was around 9.2 billion. So, any rationale on the borrowing which was done in the quarter and what was the cost of that borrowing?

Ashutosh Khajuria: These are the Treasury operations basically. So, you will see borrowings, you will see the deployment and that is to capture the arbitrage in money market. So, liquidity wise you can see our LCR that reflects about the level of HQLAs vis-à-vis our immediate obligations. So, LCR has been consistently above 200%. So, there is nothing on the liquidity side and partly because of the granularity of liabilities. So, don't look at one item in isolation. You have rightly picked up both from both sides. So, it's basically because of the arbitrage operations. There is no long term borrowing in the balance sheet, other than the past refinances, which are depleting. It's also around 78 only

Gaurav Kochar: Is it fair to assume the spread we are earning here is much lower than our business spreads and hence it's a drag on the reported margins.

Ashutosh Khajuria: In treasury operations you'll always have an interbank market spreads, interbank spreads are not going to be same as your business.

Gaurav Kochar: That's what I'm coming to. There's an arbitrage right now, but going ahead once the liquidity eases, can that translate into at least the optical margins to improve which right now in the 320 margins that we have disclosed, there will be a lag because of this, but once this get normalized and the borrowings and both the liquidity ease off from the balance sheet, can we assume this translate into an uptick on optical margins, 3.2 becoming higher?

Ashutosh Khajuria: The total impact of this is not much when you see it on a particular date on the level of assets and all. It's an ongoing thing. And capturing the arbitrage is the smartness of the treasury guys to look at spot those arbitrages and capitalize on them. As long as these arbitrages are available, treasury operations would be there, but you can't draw a trend line on the basis of that.

Gaurav Kochar: Maybe quarter end phenomenon, that's why this looks elevated. Sure, I got your point. And my next question is regard to the employee expenses. In the current quarter we saw 5.7 billion. I know it's hard to guess future, but is this sort of steady state run rate of 5.7 billion going to remain at least for the next two quarters, is there any one-off element in this quarter or this is fully what we will see in the next subsequent quarters?

Ashutosh Khajuria: I think Shyam has already touched something on that. See, these would depend on your pension liabilities and your pension liabilities are being actually passed on to LIC, I mean, in our case, it's mandatory to buy annuities, you buy from LIC or any other annuity sellers like HDFC or SBI and so on and so forth. So, these are some of those institutions from who we are mandatorily required to buy annuities to pay these pension, that's what Rule 89 Shyam was referring to. So, we can't manage pension requirements or so. So, when annuities are to be bought, these are all function of where the yields are moving. So, if interest rate cycle goes up and all, our liabilities here would reduce because then you will have to pay lesser for your annuity. I hope you understand that. So, for buying every one rupee per month today, if we are paying Rs.160 which was Rs.135, about two, two and a half years back. So, once again, if the interest rates move up, that would go down, you will have to pay a lesser amount for buying every one rupee pension per month.

Shyam Srinivasan: Summary is we expect this 570, 575 to be holding for Q3, Q4.

Gaurav Kochar: On the fee income side, I think we saw very good traction this quarter and I saw cards fees around Rs.75 crores. How much of this would be credit cards? I know we started the product late in the quarter.

Shyam Srinivasan: Credit card is too small. We just started with the debit. We are now a leading debit player in terms of spends, and that's debit-led.

Gaurav Kochar: In terms of the tie-ups that you've done with fintechs, what kind of fee income run rate can we assume going ahead, I mean, this kind of momentum, can we assume this will replicate in the coming quarters?

Shyam Srinivasan: Core fee income momentum, we are seeking to keep this and keep improving, not just by the fintech partnerships, our organic business model is that. So, a fintech related outcomes for this financial year parking, everything we're saying is an FY'23 outcome.

Moderator: The next question is from the line of Abhishek Murarka from HSBC. Please go ahead.

Abhishek Murarka: So, a couple of questions. The first one is, you said that you're looking at 1.2% ROA to your top line, and currently you are at 0.9%, and you're also saying that 3.2, 3.25 broadly there, your credit costs are among the lowest historically. So, where does that come from?

Shyam Srinivasan: We've said this for our business mix, our credit costs, there is optimum to make another five basis points everywhere. So, it's not going to be one little thing and there's no one silver bullet, it's a little bit of everything done consistently. And if you model that this 1.2, 1.25 is possible given the mix of business that is shifting. Credit cards is just picking up, commercial vehicles are just picking up you saw pick up in business banking and commercial banking, gold loan was muted this quarter, PL has been muted. So, these are six businesses which have higher business model. And credit cost for this quarter was a little muted, credit costs on a generic basis is even 65, 70 basis points. I'd like to improve that by 10 basis points; 70, 75 basis points improving it by 10 basis points.

Abhishek Murarka: These new businesses that you are doing through BC. So, in this context, what I wanted to know is the new businesses you're doing which is credit cards what AUM target kind of scale do you see in these businesses in a couple of years, just broadly what is an aspirational target?

Shyam Srinivasan: We are not certainly going to become India's largest bank or anything like that. As I mentioned earlier, we're looking at initially an existing to bank customer profile and then build it into the new to bank. So, if in a two year period we are getting close to say 12, 15 lakh cards, we've done well and then the dynamics kick in for us. Likewise commercial vehicles we've just crossed 1,000 crores, we will build it about 5,000, 6000 crores in two years' time. Commercial banking, business banking put together is about Rs.26,000 crores. We think that has potential to go up to Rs.40,000, 45,000 crores.

Abhishek Murarka: From microfinance?

Shyam Srinivasan: We are pursuing organically. Inorganically we have none on hand. I've always said if there's something, we will be very happy to look at it. But unfortunately, nothing on hand just now. We have not taken eyes of that. There will be something that will come up in the next few quarters. I did say in the last call, we want to see how the environment is playing out. I think they're just getting some stability. So, we'll watch for another quarter.

Abhishek Murarka: And the second question is slightly connected to these digital personal loans. Last couple of quarters it's been coming off. First quarter, I understand, but second quarter also there's a sequential drop. So, can you explain why that book is contracting and what's the outlook there?

Shyam Srinivasan: It's conscious. In the current prevailing credit environment, if you offer easy to take credit, you may end up becoming a problem. So, we're just watching for it. As we go into Q3, we'll pick it up on that.

Abhishek Murarka: In that book, what would be the cut off let's say customer profile in terms of let's say CIBIL score or something like that?

Shyam Srinivasan: I think it's not just one. We create our own score including CIBIL score. We look at past performance record on that. It's a largely cross sell to existing liability base. So, we have an internal score based on how we model the client profile and based on experience we keep experimenting at various price points, but before delivering the credit, we scrub the bureau.

Abhishek Murarka: Just these fintech tie-ups, what is the run rate of SA accounts or the throughput of SA accounts this quarter?

Shyam Srinivasan: I said we've done about 3 lakh accounts with both the fintech partners this quarter. This is little filtered as in we check a tap, we disallow and allow at different points of time depending on volume, but I did say in the last call, right, in a normal day we do about 3,000, 3,500 accounts normally. Now we are running at 7,500 accounts a day.

Moderator: The next question is from the line of Ajit Kumar from the Ambit Capital. Please go ahead.

Ajit Kumar: A couple of questions from my side. First what would be your total SMA smart book now? I believe last or last to last quarter it was 4.6%.

Shyam Srinivasan: The SMA-1 and 2 is now close to 2% and SMA-0 is about 1.82%, little shy of 4%.

Ajit Kumar: So, roughly 50, 60 basis points improvement on QoQ basis?

Shyam Srinivasan: Little better, I think last count I saw 67 or 70 basis points.

Ajit Kumar: Second is on restructuring. So, just wanted to reconcile the numbers given in presentation and in result as part of notes to account. So, as per presentation the total restructuring is Rs.3,553 crores with COVID specific restructuring being Rs.3,423 crores. Now as per notes to account, point #12 format B table, I believe that is the format in which you report to RBI, the total restructuring done is roughly Rs.2,700 crores. So, where is the disconnect actually of this, if you can explain? There is a gap of 700 crores.

Babu K A: Just for your information, in the disclosure MSME is not included, excluding MSME only disclosed, that is why it's different.

Ajit Kumar: If you can talk about your partnership with OneCard as far as your credit card book is concerned, any qualitative comment, what is the purpose of this partnership?

Shalini Warrier: This is actually a continuation of our entire journey on partnerships with fintechs. So, as we have partnerships on the gold loan side on the microfinance side, on the savings bank account side, as we've launched our credit cards, we've looked at partners who can work with us to acquire credit cards from the market and that's how our partnership with FPL is structured. It's a partnership where the entire acquisition and servicing is done by the partner. Obviously, the booking is done by us. The credit criteria are determined in conjunction with us and they go through a filtering process and they come on book. So, it's a part of that overall strategy to expand our presence in the market through fintech partners. It's about a month old now and booking at a good rate of 200 to 300 cards per day. We are going to scale that up now as we have got greater confidence on the technology capabilities and the interfaces that happened. It's actually can't be seen in isolation of everything else that we're doing on fintechs.

Moderator: The next question is from the line of Nitin Agarwal from Motilal Oswal Securities. Please go ahead.

Nitin Agarwal: A few questions like one is onto the OPEX, like have we fully reflected all the changes on the OPEX in this quarter and what will be the run rate in the coming quarters? And related to it with a change in accounting treatment which has driven the sharp rise in cost-income ratio, what number should we now be looking at on the cost-income ratio because this is one metric that's really quite focused and we've been giving guidance, so what is the revised sort of guidance on this

Shyam Srinivasan: I'd like to keep one more quarter to understand this better but I think now getting to 52 to 53 would be our first milestone by the end of this financial year closer to 52. And then as income picks up hopefully next financial year, trend to 50, but at this point in time I'd guide for 52.

Nitin Agarwal: Everything is now reflecting in OPEX like the increase because of the rise in pension contribution?

Shyam Srinivasan: You would have seen that now, Nitin, Rs.177 crores is the family pension impact which will amortize over five years and that's the view, if possible, we'll do it much earlier but over five years. So, the incremental impact per quarter is about Rs.25 crores or Rs.30 crores.

V Venkateswaran: There is a disclosure, note #13.

Nitin Agarwal: On to the margins, so what will make us more constructive on margins like we have been talking about 3.15 to 3.2 range but if I look at like our CASA has grown around 500 to 600 basis points in last 18 months, it is growing at a faster rate already and likely to expand further. So, what will make us like report a higher margin from here?

Shyam Srinivasan: Nitin, I know, I'm not going to be popular in saying this but I think chasing margin in itself is never a good strategy. Mix of business, credit quality have to be factored in. So, I would say when I guide for 320, 325, 330, we have factored that and I mean we don't have a path to say I can guide 340, 350 without taking disproportionately high risk which at this juncture we don't have the appetite to achieve.

Nitin Agarwal: Lastly, on to the restructured portfolio like any sense you can share as to what proportion of the restructured book is like going to turn into bad loans and what proportion of it is under moratorium right now because last quarter you did talk about that the collection efficiencies in restructured book is as good as a standard portfolio. So, how that…?

Shyam Srinivasan: I don't think that changed. I think in our disclosures we have made it, right, 75% of the book is LTV and 73% is 100% secured, collateralized. It's largely retail, home loan, loan against property book that we have restructured. We are quite pretty comfortable that it's not going to be a run-away problem. And over a two, three year period, maybe 20%, 25% of the book will slip and which will then be our commitment to the 65% PCR hold which we have started building a provision cover over that and we are now almost like 440 or 450 crores provision already built on that book and in the coming two quarters also, we will build. So, we will exit the year in such a way that in the two financial years ahead, even if we see 20%, 25% slippage in this book, we can still hold our 65% coverage.

Moderator: The next question is from the line of Harshvardhan Agarwal from IDFC AMC. Please go ahead.

H Agarwal: Just wanted to understand like on the fintech hires that we are doing, are they actually seeing traction on fee income and on slide #27, we have a breakup of fee income line wise, where does all the fee income that we get from fintech will sit?

Shyam Srinivasan: Fintech fee income is not separately reported. That will come under our debit fee income. Fintech build at this juncture, we are monitoring the account performance on a three MOB basis, how balances are built. If you were to originate through a normal digital channel versus this, we are tracking almost just the way our normal digital account would behave.

H Agarwal: And sir, we do have a tie up with ICICI Securities for a 3-in-1 trading account. How is the traction there and with a tie up what kind of revenue that is generating for us?

Shyam Srinivasan: While we don't declare individual partnerships, you can see that generally our fee income traction is positive, driven by a range of activities, one of which is a partnership with ICICI Securities.

H Agarwal: So, sir, in this ICICI Securities or any of these tie ups, we do keep the float in the account and we do earn income on that, right?

Shyam Srinivasan: Where the deposits is there, float income will be ours.

Moderator: The next question is from the line of Bhavik Dave from Nippon India Mutual Fund. Please go ahead.

Bhavik Dave: Two questions; one is similar to the previous question, wanted to understand if you can give us some clarity on what exactly this fintech tie-ups mean for us because there are so many of them and we are trying to achieve a lot of things like the credit card fees, acquiring accounts by Neo, so just want to understand exactly how are we going to monetize them? And second question is related that the other expenses that we have around Rs.900-odd crores that we did for the first half. How much would be due to these partnerships or how much of it is linked to business growth, so how much will it be variable that as and when business picks up for us, the business that grows, so just want to understand the variability of that other expenses?

Shyam Srinivasan: You have two questions are interlinked. Our OPEX increase this quarter versus the previous like somebody pointed out was Rs.48, 49 crores. Significant part is because of the variable. And in the variable comes the new account sourcing which includes the accounts that we source through our fintech partners. So, in some sense, you have to see the fintech partners at three layers; one is the partnership where the acquirer for us is like BC, so there is a BC cost. The second is we are a service provider for them and then there's a certain degree of acquisition cost that we bear. So, the fintech partnerships as we see it is if we were to open 1,000 branches and book another 3,000 accounts a day versus using our partnerships, using technology and getting to a new client base which normally we may not be directly getting because this profile of customers doesn't use physical brick-and-mortar, they look from a cooler stuff, we are using a front-end which is more cooler and contemporary. So, our fintech partnership speaks to our theme of "Digital At The Fore, Human At The Core," Branch Light Distribution Heavy. That's why we are investing heavily into this in terms of partnerships, focus by senior people, giving a time, attention, upgrading the back-end capability so that it is highly resilient and be able to give the quickest turnaround to those customers. How will it play out? It takes a good year to understand that. Early signs are very positive.

Bhavik Dave: What we are trying to do is we are trying to get newer segment of customers via the fintech partnerships, right. We already have 8.5 million customers on the liability side or debit card side. The incremental customers are reasonably different in terms of the profile meaning maybe 30-years and below, more millennial like customers or salaried, is that what we are trying to do with these partnerships because we already have a reasonably high base of customers to mine for our existing personal loans and credit card side in some sense?

Shyam Srinivasan: Absolutely yes.

Bhavik Dave: So, the 3 lakh accounts that we source via this fintech, are reasonably younger set of customers, is that a fair way to think about it?

Shyam Srinivasan: Younger, I don't know if age is a criteria, but younger and their dispensation to life you could say.

Moderator: The next question is from the line of Mahesh MB from Kotak Securities. Please go ahead.

Mahesh MB: Just a couple of questions from my side. One, recovery was reasonably strong this quarter. If you kind of give us some color how are you seeing the second half of financial year? And is there any blind spots to be worried on the Corporate side from here on?

Shyam Srinivasan: Yeah, this quarter was strong, largely because Q1 was muted, even the first 45-days was relatively low, so we saw higher slippages, usually from a fresh slippage pool, recovery is usually stronger, we saw that. We believe that this run rate not maybe the Rs.400 crores but a good steady state would be somewhere in the Rs.300, 350 crores and that we will certainly focus on. On the blind spots, there will be some that will slip over periods of time. Nothing looks to alarming at this point in time, we don't have any single big ticket which is in the 50, 60, 100 crores which is a problem, but I am not flagging any risk that should cause anything. We still think that Rs.400-odd crores which used to be a normal slippage in a quarter, that's a number we should focus on.

Mahesh MB: On this Kerala impact of COVID or the floods, doesn't have any major impact right now?

Shyam Srinivasan: We have managed this portfolio for many years quite sensitively.

Mahesh MB: Again, on the OPEX line, just wanted to understand with the larger parts of your businesses now moving to your subsidiary, ballpark assumption, if you were to double the balance sheet on the retail side, do you think you need to put in a fairly large number of employees to match that or you think you are in a position right now where your existing employees can start contributing on the revenue side a lot more meaningfully as compared to where it was earlier because the OPEX has moved to the subsidiary?

Shyam Srinivasan: I think our employee addition for many years has been very muted. If I look back four years, our net addition in employees is only about 600 people while our business is probably more than doubled so to say. So, I think…

Mahesh MB: That doesn't change even today is a fair assumption to make. There is still a lot of headroom available?

Shyam Srinivasan: Yes, productivity, digital, efficiency very much there.

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

Krishnan ASV: My first was just a repetition of what Mahesh asked around the recovery environment. So, while this was a one-off and it kind of made up for the loss of half a quarter last quarter, just wanted to understand in general the recovery environment plus you had an exposure to Air India moving from weaker hands to stronger hands, does that make a difference to how you look at that particular exposure specifically?

Shyam Srinivasan: Air India is now on guarantee, a very small amount.

Krishnan ASV: But in general, the recovery environment do you think is something that helps you get to a 300, 350 crores?

Ashutosh Khajuria: Environment has certainly improved. That shows in the recovery and upgrade.

Moderator: The next question is from the line of Jai Mundhra from B&K Securities. Please go ahead.

Jai Mundhra: Sir, first question is on ECLGS. A) if you can quantify the outstanding number that we have? And secondly, July to September they would have completed the first year of moratorium. If you can share your thoughts once these accounts have come out of moratorium, how are they behaving or how should one look at the stress from this portfolio?

Shyam Srinivasan: The repayment this quarter was bang on. So, we didn't have any stress on that. If we can forecast that for the remaining quarters, we are a very happy team, but that is hard, but at this point in time the ECLGS portfolio is very small, repayment was good. Book restructured in total ECLSs book is nearly Rs.3,000 crores. But with the new announcement, there would be some more disbursement, but as of now it's there?

Jai Mundhra: Sir, the question is so far anyway this portfolio was under moratorium and maybe in the latter part of this quarter, you would have seen some accounts coming out of moratorium and…

Shyam Srinivasan: Correct, that's what I said, their repayments were perfect.

Babu K A: Yeah, 17% of the book has come in demand bucket and we did somewhere around 95% collection. Absolutely, there is no challenge particularly with regard to the moratorium or restructured books of the demand bucket.

Ashutosh Khajuria: In short, I think if we can sum up, our recovery percentage in the restructured book is quite similar to the general book.

Jai Mundhra: Second question is on restructuring the nomenclature. So, let us say you have restructured Rs.2,000 crores of retail. If a customer has taken a prudential restructuring, he wants to repay on time, he can still do. Is there any clarity that by what milestone would you untag him from restructuring?

Babu K A: Restructuring is done for 24-months, that is the maximum tenor that is permitted. After this 24-months, his account will untag for the restructuring book if it is not turning into NPA by the time.

Jai Mundhra: So, even if he has repaid some amount of it ahead of his schedule…?

Babu K A: It will remain standard restructured up to the end of this 24-months, that is the maximum tenor.

Ashutosh Khajuria: I think in the past there had been so many restructuring done under CDR, this, that and all. If you see, we always present to our analysts and investors the slide on which we show the path of restructuring. Earlier, we used to continue till it is fully repaid and all. And that's what you would have seen in graph. That amount used to be Rs.3,200 crores and all and gradually it had fallen to Rs.600, 700 crores. This is a special restructuring that has happened under COVID. Two years is a moratorium period. We will watch it after moratorium is over how long it is behaving properly because these are mainly housing loan accounts for 15-years, 20-years, 25-years or so. So, maybe after two, three years of satisfactory performance post moratorium, we will remove the tag but that we would share with you through a slide and all that so much we have taken out of that book. Even otherwise sir, it remains a standard bucket. Yeah, yeah, it remains. I am talking of removing that tag of restructuring. So, I think that trend should be there. Post moratorium, we will watch it for a couple of years or so and then disclose that this is what we are removing from restructured bucket.

Jai Mundhra: I missed your comment wherein you said that you have done some relapse from outstanding restructuring and then we have made some over and above IRAC provisions. So, if you can elaborate sir, if you have any then provisions on the expected restructuring or did I hear it, right?

Ashutosh Khajuria: We are expecting that maximum slippage could be 30% from this. This is a sort of very conservative estimate. The number could be much lower later on. But assuming that it is 25%-30% slips and all, on that we need to have 65% PCR which is what we have been maintaining for last so many quarters. So, if we have to maintain 65% on that 25%, 30% of restructured book, then how much provision we need to hold. So, on that, I think Shyam has shared, we are already holding Rs.450-odd crores and we will gradually build up because post moratorium then we would actually be knowing whether it is slipping or not. So, for that in advance, we are building up the provision, and that's what management outlay. We already have additional provision made in this quarter itself.

Jai Mundhra: So, Rs.450 crores is the restructuring provision outstanding, right?

Babu K A: That is the correct outstanding provision for RF1 and RF2 for the Bank

Moderator: The next question is from the line of Gurpreet S. Arora from Aviva Life Insurance. Please go ahead.

Gurpreet S. Arora: In your opening remarks, you mentioned you have done around Rs.1,000 crores of restructuring. I think the guidance for this quarter was Rs.400-odd crores. So, where has the incremental surprise for us come from? Second, if you could maintain the slippages guidance for this year as FY'20 levels plus/minus 10% which you alluded last quarter?

Shyam Srinivasan: I think you picked up half of my statement, you only picked up my restructuring comment last time of about Rs.400, 500 crores, but you don't pick up the slippage part; slippage is half of what I thought it would be. So, on balance, between the two slippages and restructuring, this quarter is also roughly about Rs.1,300 crores, not very wildly off from what we had visualized. The good news is slippage didn't happen. Even better news is the customers who opted for restructuring are secured and therefore that's the blend that we see. To your second question, full year slippages we had topped off somewhere equal to what it has been for the previous two years which is roughly Rs.1,800-2,000 crores. Current trend line suggest it could be meaningfully better.

Gurpreet S. Arora: If you can comment a little bit on the business environment especially on the SMEs and any sort of cautious industries or geographies you wish to highlight?

Shyam Srinivasan: That's a very geography-sensitive or sort of sector-sensitive and it keeps varying but we generally kept off hospitality and those that are heavily contact sensitive, right, obviously. And that's why our slippages are in well in control because for a year we have kept away from those segments, that will continue. Business environment, certainly better than what it was say most of last financial year, last quarter was good and the quarter that went by for period starting I think August onwards we have seen momentum. I am quite confident that second half we will see much higher growth than first half.

Moderator: The next question is from the line of Rishikesh Oza from RoboCapital. Please go ahead.

Rishikesh Oza: If you could give any guidance on credit cost and loan book?

Shyam Srinivasan: Loan book I just mentioned that YoY we have grown 10%. We think now business momentum picks up, somewhere in the teens in this financial year is possible. We are pushing for higher but we are somewhere in the teens. Whether it's mid-teens or high teens we will see in a quarter, quarters ahead. Credit cost this year will be a kind of a mix because Q1 was high, Q2 was nil. So, let me not comment on it. Suffice to say our overall full year credit cost somewhere is in the 70 basis points, 80 basis points you should factor for.

Rishikesh Oza: And next year?

Shyam Srinivasan: We will give you guidance closer to the year.

Moderator: The next question is from the line of Franklin Moraes from Equentis Wealth Advisory. Please go ahead.

Franklin Moraes: Could you throw some light on the outlook for Fedfina?

Shyam Srinivasan: They are doing well. They are focused exclusively on small ticket size credits; LAP, gold loans, small business lending and we are quite happy with the progress.

Franklin Moraes: So, in terms of growth if you could share whether they will also be growing aggressively?

Shyam Srinivasan: Through the pandemic, of course, we were all watchful and the credit standards are good and the book is now at 5,000-odd crores and I think they are positioned for growing at maybe like 30% a year or more, they are doing well.

Moderator: The next question is from the line of Nilanjan Karfa from Nomura. Please go ahead.

Nilanjan Karfa: Just one question on this remittances where we have done a phenomenal job. Just checking, this is the amount which flows into our deposits, we are not actually originating it, is that how you measure it?

Shyam Srinivasan: No-no, this is money that flows through the pipe and comes through as remittances, not all of it become my deposit, I would love it, part of it becomes. The end beneficiary could take the money and take it away for end use which is not placed in the bank. This is money that flows in through us. We are a pipe for that money to come in. As a part of our management, we try to keep a large part of it, we encourage the customer to bank with us.

Nilanjan Karfa: Therefore, in that context, I was just looking at that NRE deposit, right. I think this is the first time that QoQ had a decline in the September quarter. Does it point to anything about utilization of these or any sort of weakness in the environment or we will just too much of the….

Shyam Srinivasan: Maybe Shalini or Ashutosh can give a better color, but generally I wouldn't read much into it simply because that usually is when the Onam comes and also the last four months have not been the best period for non-resident side. So, to that extent, movement of money may have been lower. Now, we saw in October rupee became 75 and…

Ashutosh Khajuria: Shyam, I was about to say that. Actually, it's a function of how the exchange rate behaves…

Shyam Srinivasan: After the rupee became 75, the floodgates were opened again.

Nilanjan Karfa: On the restructuring, roughly what kind of moratorium have we given or when should we start looking at large bulk of restructuring to come through and the repayment….?

Shyam Srinivasan: I think Rs.3,500 crores over the next nine quarters is divided in different segments with about Rs.800 crores due in repayments in next year first quarter, right. Babu, is that the number if I recall, right?

Babu K A: By Q2'23 the demand book maybe somewhere around 80% of the restructuring.

Nilanjan Karfa: When do we see the new investments that you are doing on the retail side to start showing up in the profitability numbers?

Shyam Srinivasan: I think they are all showing up in its own little ways every quarter. You saw fee income pick up nicely. I think every quarter you will see. So, I am not committing to…this is the bank philosophy, not mine and we have lived up to it, we will stick to that, we don't promise something which we…we don't have silver bullets, others do have, we don't have.

Moderator: The next question is from the line of Madhu Gupta from Quantum Advisors. Please go ahead.

Madhu Gupta: My first question is what percentage of the employees are on the defined centering plan which you expect they will retire by FY'24 and what are the kind of cost savings that will accrue to the bank as a result of that? There have been some reports that you plan to list your subsidiary, Fedfina. So, could you give some more color on when it's expected?

Shyam Srinivasan: On the pension, we didn't say the last of the employees. The last of the employee will retire in 2047 or whatever. But large number of the people who were onboarded before April 1, 2010, majority is year '24, '25, and after that it will taper down. So, to that extent, our annual pension cost is roughly Rs.400 crores incremental that we have been providing for the last say four, five years. That should see some improvement of at least 30% of that in the period starting '24. On the second, we also read some press articles that you said, so I really have no comments.

Madhu Gupta: There are no plans of listing as of now, not confirmed now?

Shyam Srinivasan: Where something is required to be announced, we certainly will.

Madhu Gupta: Last year you had said that there have been some slippage on account of the exposure that you have with the UAE Exchange of 1.75 billion. What is the status right now -- have the slippages increased or there is some kind of recovery over there?

Shyam Srinivasan: That's fully provided. We have not got any recoveries as yet. We are working through it. We have the security, but it's a very complex legal process that is underway. At this point in time, I have no incremental update other than the fact the process to recover is underway, we have fully provided.

Moderator: As there are no further questions, I would now like to hand the conference over to Mr. Anand Chugh for closing comments.

Anand Chugh: We just thank everyone for joining the call and I wish you happy Diwali, happy Christmas and happy new year in advance.

Shyam Srinivasan: Yeah. Thank you very much.

Ashutosh Khajuria: Thank you.

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