"Federal Bank Limited
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Moderator: Ladies and gentlemen, good day, and welcome to the Q2 FY '24 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 star, then zero on a touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Souvik Roy, Head, Investor Relations, the Federal Bank Limited. Thank you, and over to you, sir.

Souvik Roy: Thank you. And ladies and gentlemen, thank you for joining us on this busy results afternoon. We hope you've had a chance to review our latest quarterly results. It's my pleasure to share that we have had an outstanding quarter, and I would like to highlight some key points. First and foremost, we have reported broad-based growth across all segments and businesses, which is a clear sign that our strategies are yielding positive results. In particular, our net profit number for this quarter is the highest we have ever achieved.

Our ROA continues to trend well. And our ROA certainly underscores our commitment to efficient and sustainable operations. We have also successfully completed a significant capital raise in Q2, which now bolsters our financial position and allows us to pursue growth opportunities more aggressively. I'm also pleased to report that our NPA numbers remain well under control, which is a testament to our prudent risk management practices. Overall, we can confidently say that this quarter was a good one for us and the positive momentum continues.

To provide further insights and discuss these results in detail, we have our entire senior management on this call. And I'll now hand over the call to our MD for a more in-depth analysis and to answer any questions you may have. Thank you again for being a part of this call. And please feel free to ask any questions that you may have as of now. Over to you, sir.

Shyam Srinivasan: Thanks, everybody. Good evening. This is Shyam here. Like Souvik mentioned, the entire senior team is there. We'll be happy to answer questions. I think the key messages, he did read them out, but that just reinforced the fact that many of our initiatives -- I think this is a sigma of all our initiatives coming together quite well. Over the last six, seven quarters, sequentially every quarter has been a strong performance.

In Q2, environment continued to be challenging, as it is likely to be for the periods ahead in certain areas. We've seen good progress on all accounts. Credit and deposit growth has been quite consistently good. I do believe, structurally the deposits market has changed probably globally, certainly in India, certainly for us. And not daunted by that, we are reorganizing ourselves to make sure that through this period also we will be able to grow and expand both the balance sheet and also the quality of assets.

And this quarter is a good testimony to pivot that we've had in terms of kind of businesses that we are ramping up on, with a keen eye on the credit quality being intact. Notable in Q2 are the features that Souvik just spoke and the provisional results that we had shared early in the part of the quarter and the results that we announced today. The NII for the quarter grew quite smartly, in fact it grew 7% sequentially. Credit grew about 5%. Evidently, the higher yield businesses are beginning to make an impact on the overall numbers. And we do think that will sustain.

Fee income for the quarter and generally in the trend lines has been quite encouraging. And here, again, our philosophy of being a -- moving from being a pure lender to a banker, particularly as we seek out our business model, just at the cost of repeat, is about getting the better risk-weighted clients, pricing competitively, but asking for more business from the same client through I think the last two, three quarters are beginning to show results.

Earlier in the financial year, when we were meeting some of our potential investors, I explained the theory of trying to migrate from being a pure lender and being a peripheral banker to a more important banker, we are seeing traction on that account. Fee as a share of assets is almost near 1%, and we believe we have a path to get to 1.1% or better in the coming years.

So the environment for deposits continues to be challenging. Our term deposits have grown remarkably well through the quarter. Y-o-Y grew 33%. Domestic savings has gone reasonably well at about at our market kind of growth rate at 11%. What traditionally used to be a materially big part of our portfolio and our savings is seeing degrowth in some sense. We also quickly and constantly keep checking to see how the NR performance is.

Remittances have moved up materially. Our share has gone up substantially. So there is a pivot from NR savings to NR term or NR business money going into consumption and/or investment and/or setting up a new business and/or paying off loans. So there's some structural change happening and we have organized ourselves to make sure that we get more prominent in the domestic business.

We've seen good footprint expansion, and our fintech partnerships, particularly on deposits are beginning to give us some domestic savings increase. So on balance, Q2 has been good. We have seen progress on all accounts. There are challenges in terms of growth in deposits at a price. We have organized ourselves for that. And at the beginning of financial year, we did say that H2, we will see a pickup in margins.

We had also said that our dip in NIMs will be faster than the other, which it did. I do believe we've topped out our NIMs and the increase can happen here, too. So having said that, I must quickly add that the rate of growth of expectation in terms of NIM expansion will be more moderate. I don't believe some of our numbers that we visualized to get to 325 full year maybe a touch -- and this is using the old compute. We have recomputed at present both the old and new formula.

Our new formula assumes net earning assets. So you will see our NIM showing as 322, but in the spirit of full transparency, we have showed it's equivalent in both formats, so that nobody needs to worry whether the bank is trying to outsmart and trying to show different formats. No, we are representing both formats. But here on, we will present with net earning assets, which seems to be consistent with market practice.

So this expansion, from here on, we do believe, will be inching up, but the level of inching up, I'm not yet able to digest or comment, probably because cost of deposits is yet to defer down. Though Q2 versus Q1, the rate of increase was consistent, it was not much higher. Yield on advances has moved up from 7 basis points in Q1 to 14 basis points in Q2. So that trend line is quite encouraging.

So let me just pause here with the following messages. Growth, 18%, 20%, quite possible. Credit quality holding well. ROA and ROE expansion on track. We believe, we've been growing quite smartly on our net profit and traction has been strong, and we believe that will consistently hold. And the pivot in some of our high-yield businesses is working well. Deposits continues to be a higher cost item and we are organized for that.

So let me just pause here, and team and I will be able to answer questions or clarify anything that's required. Thank you very much.

Moderator: Thank you very much. We will now begin with the question-and-answer session. The first question is from the line of Gaurav Kochar from Mirae Asset. Please go ahead.

Gaurav Kochar: Congrats on the quarter. I have three questions. Firstly, on margins. I think Shyam sir alluded to the movement in margins here too. I just wanted some sense on the cost of funds repricing. In this quarter, we have seen around 20 basis points kind of repricing. So is it done fully now? Or there is still some repricing on the cost of fund side, which is yet to come in the third quarter?

Shyam Srinivasan: Venkat, do you want to go?

Moderator: Mr. Venkat is not yet connected. We are trying to connect him.

Shyam Srinivasan: Okay, fine. Okay. I think the rate of growth of deposit cost is beginning to moderate, but I think Gaurav it will be a little more contingent on how the environment is shaping up. It has certainly not yet cooled off. So to that extent, we have to be ready for one quarter or two quarters of more higher cost of deposits, because the bulk of -- as you would have noticed, this quarter we grew our deposits Y-o-Y 23% and 97% is core deposits of that, and a large part is in term. Term grew 33% Y-o-Y.

So there is money, but it's at a cost, and given everything that we are facing in the market, we believe, we should tank up when the money is available. Of course, we are finding alternate ways to ensure that the blended cost of funds is in control. That's why, I caution saying that the increase in NIM that was visualized cannot fully play through. But certainly, it is started improving, the trend line has reversed for us. In Q2, it improved, and we think it will improve in Q3 and Q4, too.

Gaurav Kochar: Sure. And just on the yield on advance bit, you pointed out that the higher interest-bearing assets are sort of seeing improved traction. And as a result of that, the yields have improved 14 basis points. So we'll be taking a step further. Let's say, the mix improves by 100 basis points. What is the delta we get on the margins?

On one of the slides, you've disclosed that on a Y-o-Y basis, there has been a 300 basis point improvement in the yield on assets or interest income coming from that asset. So I just wanted some context, for every 100 basis point kind of improvement in mix, what is the delta on margins?

Shyam Srinivasan: We should see similar kind of traction, the higher yield businesses, as they grow. But here, again, I'm cautious saying these are businesses that also have higher risk associated. So we have been quite watchful about it. But yes, so for the increase in NIM and the increase in yield on advances, we saw sequentially 7 basis point improvement. So we think that kind of momentum going into the second half also will sustain.

Gaurav Kochar: Got it. Thanks. On the opex. My second question is on the other opex bit. There was a sequential jump of around INR100 crores. I see that you've added around 23 branches in this quarter, but just wanted to get some sense, what was this INR100 crores incremental about? Was it largely because of branch expansion, or some of it was one-off? Just wanted some color on this.

Shyam Srinivasan: No. There is no one-off in any large debt. It is sequentially many things that have -- volume increase is a material part. The branch expansion is only one element. All of the full-year branch expansion code will play and the cost will play through. It's a mix of all the businesses that are growing. And there is a volume-related expense. There is the marketing and spend increase that increased about INR15-odd crores. Even the festive season, we had some very aggressive field related events. So it's a blend of a few things. I don't think there is any one-off expense sitting there.

Venkatraman V: I can come in here some. Gaurav, this is Venkat. This is largely volume-related increases in the opex which you have seen. There are no one-offs in that. And like Shyam said, some element of marketing. Branch-related cost is not a significant sum in this increase.

Gaurav Kochar: Okay. Got it. So fair to assume this run rate would continue in 3Q, 4Q, something more than this given the volumes, if it grows beyond what we did in…

Shyam Srinivasan: Assuming the same growth in credits and NII, we should continue to see similar increase in variable cost.

Gaurav Kochar: Got it. And on the fee income bit -- I mean, the last question that I have on this -- we did about INR660 crores in the second quarter. Given the third-party related fee and even generally, the volume-related fee is much better in second half. Is it fair to assume that our fee income -- because if I look at last four quarters before this, we did about INR540 crores of fee income. This quarter, it has jumped to INR660 crores. So just wanted to ensure that in the next two quarters also, can we expect a similar INR660 crores kind of a run rate or more given that second half is typically better?

Shyam Srinivasan: Gaurav, I'd say there are no one-offs in this. The lender to banker strategy is playing through. Most of our corporates and retails customers are concentrating, are giving us a larger share of their business. So we are seeing -- that's why if you see slide number 19 in the deck is quite explanatory in terms of its diversity and granularity and that should sustain.

Gaurav Kochar: Sure. And just on this. The cost to income in this quarter was 52.5%. Earlier, I remember, I mean, you have guided that every year probably 100 basis point kind of improvement. Let's say, on a full year basis this year, can we see similar sort of what we did in FY '23, at least on the cost to income side, given that we've seen some inch-up in cost this quarter?

Shyam Srinivasan: Yes, there is some inching up of costs that have happened. The volume related cost has gone up. Second is some of the businesses that we do with our partners requires us to take -- the accounting requirement is all the expenses, service charges come as a cost, and the interest income -- the income accounts -- so to that extent, these are relatively higher cost to income businesses, but higher ROA.

So we've made that conscious call saying for a couple of quarters or for a period of time, we may carry some extra cost because these come at about 65%, 70% cost to income, but are ROA accretive. So we've made that call and it's visible. You will see our ROA expanding, interest income expending -- income expanding, but unfortunately, the cost also does. So until that normalizes, we may not -- we're struggling to pull back to the 50%, but that's what we are working towards. So back half, we are -- some of these expenses is still tracking to the 50%, but yes, on a blended number, the 52 number that you see is a little higher than our original assumption.

Moderator: Thank you. The next question is from the line of Mahrukh Adajania from Nuvama. Please go ahead.

Mahrukh Adajania: Hello Sir, my first question is on credit costs. So you've done a good job and credit costs are really low this quarter. Where do they normalize, as in we were -- I mean, last quarter, it was around 39 basis points. Now it's much lower. So where does it normalize? And how long do they stay so low given that high-yield businesses are also increasing?

Shyam Srinivasan: Mahrukh, this is a question that I wish I had an answer very easy, because we certainly don't want to reverse the trend of improvement, right? That said, at 13 basis points, it's particularly low. We had said at the beginning of the year somewhere 35 bps, 40 basis points full year credit cost. First half, as you noticed, blended is in the 20s. 20 basis points second half may be a little more challenging, but somewhere late 20s, early 30s is better than where we had originally visualized the year to start. I'm happy that, that trajectory will continue. We've had no corporate banking losses for long periods of time. I hope that it sustains like that, but there can always be some challenges in the market.

Second, on unsecured and granular credit, we are tracking well. Our SMA book is at its lowest in many quarters, SMA-0, SMA-1, and SMA-2. And we believe that even through this period of growth in unsecured and higher-margin businesses, it should not fall off. We are not doing new to bank aggressively on unsecured. We are doing existing to bank and prequalified data basis. So, for the next two three quarters, this trend line will continue and should be in the zone of 25, 30 basis points.

Mahrukh Adajania: Okay, sir. Makes sense. And sir, why has the recovery income dropped off so sharply this quarter?

Shyam Srinivasan: No, some parts of it is very -- if you have one good recovery, it plays out. So you can't quite model that. It's depending on when some charge-off happens and when the opportunity comes but would not put too much attention to whether it's high or low, because these tend to be sometimes opportunistic.

Mahrukh Adajania: And sir, I just have one final question, which is that -- sorry, you just mentioned that you would still end the year with 3.25% margin, which is kind of three basis points above the current level, correct?

Shyam Srinivasan: In the case of current formula of compute of 3.22%. We are working to that 3.25% one.

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

Nitin Aggarwal: Congrats on good results. Sir, a couple of questions. First is on the fee income side, if you can talk about what is this para banking really including and there has been a strong growth that we have seen this quarter on a sequential basis. So, what has driven that? Even on a Y-o-Y basis, the growth is very strong. How do you really see this?

Shyam Srinivasan: Yes. I think para banking is basically our insurance, investments, wealth management, largely these three businesses are all tracking well. Basically, higher penetration, good distribution and some level of product improvement and focus. And that's been the focus and will continue to be.

Nitin Aggarwal: Okay. And secondly, on margins, while there has been like similar rise in cost of deposits between the first quarter and now the second quarter, how do you compare this outstanding now portfolio deposit cost to the incremental costs so as to like have a view as to how the margin can trend in the coming quarters? How much is the gap rippling now?

Shyam Srinivasan: Sorry, you have to repeat this question didn't come through well.

Nitin Aggarwal: So actually, I want to understand as to how much of the incremental cost of deposits now vis-a-vis the outstanding cost of deposits, because CASA mix has been under pressure and may likely remain so. So given that over the past two quarters, the rise in cost of deposit has been pretty uniform. So how much is the gap between the incremental cost of deposit to the outstanding deposit costs?

Shyam Srinivasan: I have mentioned earlier in the call, I do believe that the cost of deposits we haven't seen the last of the story, it remains quite elevated for the industry and could remain so if the new originations of deposits are also going to be at a higher price. So somewhere in the 18, 20 basis point increase in the cost of deposits we should factor for and work our other lines to ensure the margin expansion happens and the ROA expansion happens, which is what we're doing. Some of the pivoted businesses recovery outplayed including during more high businesses, repricing existing assets, and a combination of that, and of course pursuing CA growth more aggressively in the context of our pricing line of credit and becoming a larger lender to bigger banks and bigger customers, we are able to get some CA also. The blended car outcome will be through that.

Nitin Aggarwal: Right. And sir, on the asset quality side, we have seen very strong recoveries and upgrades and things are going really strong. So what has really driven this in this quarter, the recovery number? Any one-off there?

Shyam Srinivasan: No, Nitin. I mentioned in the earlier response also, in this quarter, there's no one-off of any nature. In fact, this quarter, relatively recovery was lower than the previous quarter. Upgrades were higher.

Nitin Aggarwal: Okay. And lastly, on the internal rating of the corporate book, there is a very sharp increase, almost 500 basis points. What has really driven this? How do you see the trend there?

Shyam Srinivasan: Harsh or Ashutosh, do you want to point out on that? Harsh, Ashutosh, Souvik?

Harsh Dugar : Yes, there has been a clear focus on the A category -- BBB+ and A category customers, which is what is shown over here, which we've seen a 5% uptick. So, a very clear target is -- because AAA and AA customers, we don't get the yield. So there's a clear focus on the A rated category of customers, which is where you have seen the increase, and also an uptick in the yield resulting because of that part.

Moderator: The next question is from the line of Kunal Shah from Citigroup. Please go ahead.

Kunal Shah: So firstly, any impact of ICRR we saw this quarter? Or it was hardly -- maybe not even one basis point or so?

Shyam Srinivasan: No. The impact of ICRR was offset -- the benefit of increased capital was offset by ICRR, roughly about, both ways, about thee or four basis points.

Kunal Shah: Okay. So three to four bps on ICRR, offset by...

Shyam Srinivasan: The capital increase. We had the QIPs that came in the quarter.

Kunal Shah: Yes. Okay. So three, four basis points getting offset. Okay. And secondly, just in terms of the overall cost of assets. So maybe I think you highlighted that there is no one-off as such and more marketing related. But overall, where should cost to assets settle when we guide for, say, ROA, ROE expansion as well? Because margins not too much of improvement, credit cost would also normalize. So, would there be any triggers for ROA, ROE expansion here on?

Shyam Srinivasan: Kunal, I long said that we'll get to 1.4% ROA in FY'25. Thankfully, we are well on course much earlier and that gives us some latitude to allow for some of these spends in expansion in branches. We are upfronting some of our branch expansion. This year, we may end up doing 100 branches or more in the full year, or a little more actually. So, to that extent, we are taking the luxury of spending a little more to ensure franchise expansion happens. So, I would think the cost of assets, where we are today, can't be very much -- there will be some improvement, but not material.

Kunal Shah: Okay. Okay. So it should stay largely here, maybe somewhere around these levels.

Shyam Srinivasan: We're working to bring it to -- earlier, we thought 48% CI. Given some of the ROA expansion coming through higher cost to income on our fintech partnerships, we are allowing us that little attitude.

Moderator: The next question is from the line of Saurabh Kumar from JP Morgan. Please go ahead.

Saurabh Kumar: Sir, just two questions. One is, what would be your LCR this quarter?

Shyam Srinivasan: What is the LCR?

Saurabh Kumar: LCR for the quarter.

Shyam Srinivasan: For the quarter, 121 or 124, I'm not sure.

Saurabh Kumar: Okay. Okay. And the second is, sir, just NRI -- NRE deposits not growing? I mean, do higher rates globally impact this growth? Or will that not be sensitive to this NRE, to this...

Shyam Srinivasan: So, I think there are two parts to it, Saurabh. When you met us, we did explain. So we are -- in the NR, there is FCNR, there is NRO, and there is NRE. The remittances led businesses, which is our NR bread and butter of business, remittances are growing very strongly and our share is increasing even more visibly. However, the FCNR, we are not a big player though we are slowly putting our foot in to try and grow that. We have not seen any dips in the NR remittances in fact, it's growing.

They are not converting into deposits, either because savings -- it's growing into deposits certainly, is becoming term. Because the rate differential between term and savings is quite high, people are moving into term, or they are using it for consumption, paying off loans, starting businesses, committing to expenses that they had held back during the COVID period. Now whether this is a sustainable change, we have to see, but I think six quarters is a good period to understand that something structurally has changed.

And we are watching this, having said that, our first and biggest feed is remittance share going up, which it is for us. The second and third part, which is the NRO and the FCNR has not been our biggest strength. We are working through. May be Shalini can also give us the numbers in terms of deposit share, NR, where we are gaining share. Shalini may be you want to add, please?

Shalini Warrier: Sure. Thanks for that. So as Shyam mentioned, this is sliced into three parts, which is NRE, FCNR and NRO. Our focus has entirely been, for very long, on NRE. And there, we assume significant market share growth, roughly about 8.32% March of last year, 8.45% this year.

FCNR -- and that Saurabh kind of addresses your question also. A lot of the customers who tend to put in FCNR are the ones who are now retaining their money abroad. And some of them are obviously using that as leverage to kind of get FCNR deposits in country. We don't play too much in that space of FCNR. So on FCNR, we've actually seen a reduction in market share. NRO is not something we've been kind of working on for a very long time, because our bread, butter, jam has always been NRE.

So the short point is, FCNR and NRO is where some of the growth is coming, which we have not been playing in. Coming -- going forward into the next few months, we will be playing a large part of the market in those areas also. We will be working on those, but the bread, butter, jam really is NRE, both term and savings. We find a lot of the movement is actually happening from savings into term, and that's because the differential in interest rates is high between the two of them.

Ashutosh Khajuria: Just to add, the FCNR segment of NRI deposits competes with the global rates and all. Because there you have no exchange-related so-called gain or risk. So therefore, even with interest rates going up overseas and naturally the impact on FCNR is there, unless you are ready to pay that type of cost or make it -- because this is a fixed rate, it's not floating. On the date of contracting, for next one to three years, it is going to remain at that level. So even banks are not probably pursuing that much of FCNR deposit growth.

On the other hand, on the NRE term and NRE savings bank's interest differential, which used to be around 200 basis points, now is about 400 basis points. So as a result of that, part of NRE savings is moving towards NRE TD. And also while remittances are increasing and all, they are getting initially parked in NRE FD for our clients, and then they are being used probably even for physical assets and consumption.

Saurabh Kumar: Okay. So FCNR will not -- like in the current rate environment, I don't think -- your on-book domestic TD will be cheaper than FCNR. Would that be a fair comment?

Shyam Srinivasan: Yes. Operate and do it domestically does not make sense.

Ashutosh Khajuria: On a fully hedged basis, yes.

Saurabh Kumar: Okay. Thank you.

Shyam Srinivasan: Yes. I've said this three times already. Just to reinforce the same message. Deposits are available at a price and we have to make a call at what price and how much you want. We saw significant growth this quarter on deposits and we'll see. We grew from 33% this year, by this quarter sequentially, on Y-o-Y side. Next question please.

Moderator: Thank you. The next question is from the line of Pranav from HDFC Bank. Please go ahead.

Shyam Srinivasan: Pranav must be busy reporting his own numbers. His bank numbers are just on the screen.

Moderator: Right. As there seems to be no response from the line of Pranav, we'll move to the next question. The next question is from Rakesh Kumar from B&K Securities. Please go ahead.

Rakesh Kumar: Yes. Hi, sir. Thank you. Sir, on the MSME loan, like we have seen some reduction, some volatilities there on the sequential basis. So around INR2,000 crores like business banking plus commercial banking numbers. So could you tell us, what is the reason for this -- like this decrease from INR33,000 to around INR31,000 crores number? Especially in the commercial banking, this dip has happened. So any reason for the same, sir?

Shyam Srinivasan: Sorry, I have to pick up the slide. Where in the slide are you referring to?

Rakesh Kumar: Sir, this is Slide number 14. We have even MSME business banking plus commercial banking growth of 16%, INR31,000 crores number and similar numbers in the Q1 results, INR33,463 crores. So business banking has grown this quarter also...

Shalini Warrier: Which slide are you referring to?

Rakesh Kumar: This is, ma'am...

Harsh Dugar: I think, I got it. Harsh here. I think, what he's referring to is on Slide number 14 regarding the MSME growth being at 19%. Business banking has grown over 18%, 19% and commercial banking at 21%. The remaining portions are the non-MSME piece. What you see is the MSME piece. Commercial Banking and Business Banking is also a very small portion, which is non-MSME also.

Rakesh Kumar: No. Sir, firstly, this entire MSME book, which has come down to INR31,447 crores. So what is the reason, firstly -- so which part within that has come down? And why it has -- like is there any -- what is the reason behind it, basically?

Harsh Dugar: I'm not getting it. The MSME piece has grown by 19% Q-o-Q basis.

Souvik Roy: I think, there's some confusion, Rakesh. If you look at our presentation, on Page 14, we have mentioned MSME book at INR35,616 crores, there's no reduction.

Harsh Dugar: Exactly. There's a 19% growth.

Venkatraman V: Sorry, Souvik, just one point here. Just referring at our website, we may have to update that slide in the website. It's showing a different number.

Souvik Roy That's already updated, sir.

Management: Okay. Maybe just referring to that before the updation.

Souvik Roy: Okay, sir.

Rakesh Kumar: Okay, so there's a change in the slide. Okay. So number has been changed.

Shyam Srinivasan: INR35,616 crores, Rakesh.

Rakesh Kumar: Okay. And sir, in this credit risk weighted density, so we see -- like there is some increase there on the risk -- like especially the market risk also. Market risk number is slightly on the higher side. So is this because of the investment book growth?

Shyam Srinivasan: Your voice is not coming through. You have to repeat the question.

Rakesh Kumar: Sir, this market risk number, which has gone up slightly. So is it because of investment book growth or there is any other reason also to this investment book growth and the market risk weight number?

Shyam Srinivasan: Damodaran, are you there?

Damodaran C: This is due to growth in investments. We have certain growth in investments in NSLR book, bonds, and debentures.

Rakesh Kumar: Okay, sir. Maybe I will take it offline. Thank you, sir.

Moderator: Thank you. The next question is from the line of Madhuchanda Dey from MC Pro. Please go ahead.

Madhuchanda Dey: Hi, congratulations on very good set of numbers. I have a couple of questions. To an earlier participant, you mentioned that you do not expect a meaningful reduction in the cost-to-income ratio. And you also mentioned that you're targeting an ROA of 1.4% by the end of FY '25. Is my understanding correct, first of all, on this ROA?

Shyam Srinivasan: Yes. If you remember, when we started FY '24, we had said, over two financial years, we'll get to 1.4% ROA. Happily, we're trending much earlier. And certainly, we'll now seek to do even better. Yes, I did say that number of 1.4%, that's what we had said at the beginning of the financial year. Thankfully, the traction is good and we'll hopefully keep this momentum going.

Madhuchanda Dey: Yes. So my question is, given that the credit costs are extremely benign, can't get better from here, and your net interest margin is also going to kind of stabilize the high yield getting offset by high cost of deposits. So the only meaningful driver would be cost-to-income ratio. So given that you are saying that it's likely to be sticky, are we to expect a more gradual or virtually very little growth -- very little increase in the ROA going forward?

Shyam Srinivasan: Yes. I would think the improvement that you have seen, we should sustain them. There is opportunity to increase our fee as a share of assets by another 10-odd basis points over the coming quarters. And as we do that, by that window, we do believe cost of deposits will start trending down, which, again, is in expansion. The re-pivoting of some of our businesses will again aid in expansion.

These three elements, higher share of fee as a share of assets, deposit costs trending down or flattening out over the periods ahead, and the higher margin, higher yield businesses picking up scale, all are opportunities for expansion. And I'm sure over a two year period that we're working through, we will see even more efficiencies kick in. And the only reason we allow for a higher cost to income is only because it's ROA accretive. We are not raising businesses that are ROA decretive or on that same margin, not incremental, we won't do the higher cost to income.

So the blend is -- ultimately, the ROA expansion is the driver, and we're working through that. So at this point in time, our guidance, which is, we are not altering the guidance, 1.4%, and looking up. Certainly, we'll try to improve that in FY '25, but yes, that's the trend line. So there are levers available, but yes, there is one single lever. We have a few basis points across all parameters. And that's how we've become from 0.78% to 1.35% very steadily and consistently over five years.

Madhuchanda Dey: Okay. Got it. So is it -- I'm not asking you for a guidance, but is it reasonable to assume that from FY '24 level, given all the factors that you outlined, 10 basis points kind of an increase in ROA is possible?

Shyam Srinivasan: Which is, what we're working to, Madhu. There are no external -- Yes.

Madhuchanda Dey: I've got the answer. Thank you very much and all the best. Thank you.

Shyam Srinivasan: Thank you.

Moderator: Thank you. The next question is from the line of Kaushik Poddar from KB Capital Markets. Please go ahead.

Kaushik Poddar: See, your operating expenses in the first half, both the quarters combined, has gone up nearly 25%. And even your cost-to-income ratio is at a high of 52.6% or 52.5%. So that seems quite high. So what's the road ahead?

Shyam Srinivasan: That's what we were explaining also. I am allowing for that higher cost to income because these businesses are ROA accretive. So we have to sustain the higher cost to income because these are some of these partner-led businesses, which is like credit cards and personal loans and gold and microfinance. That's how the ROA expansion is also happening.

If they were not happening and ROA was not expanding, we wouldn't be doing that. We will be going back to our 50-odd percent, because some of these service charges are directing the expense line, that is the corresponding revenue, and the cost to income is in the 60s or mid-, almost 70s.

So that set out, our core structure is performing on course, and we are spending on certain initiatives like brand and branch expansion, both of which are good for the periods ahead. But having said that, getting to the 50% and improving in a year's time is what we were pushing.

Kaushik Poddar: You'll be able to change -- I mean, the cost to income of 50%.

Shyam Srinivasan: Yes. So we were trending closer to 49%, but some of these developments and how accounting needs to be done for partner-led business is requiring us to take the cost to income higher. But the only trade-off here is like if these are distinctly and definitely and compellingly ROA accretive.

Kaushik Poddar: Including this incremental cost for this newer initiative, so this 50% will be at the firm level, at the bank level, or you are...

Shyam Srinivasan: Yes, yes, at the bank level. Yes. Going into FY '25.

Kaushik Poddar: Okay. And this people -- I think I remember you mentioning something about the older employee pension coming off or something sometime later?

Shyam Srinivasan: Yes, that's started trending down quite substantially. By FY '25, a large part of it will start falling off, because the majority of the recruitments -- I mean, all recruitments after 2010 have been on the new scheme, so to that extent, the retirement age of most of the people prior to that is beginning to taper. In fact, the last employee of that site will retire in 2037, but the bulk will retire, have retired, retiring.

And to far extent it is linked to yields Kaushik where every time there is a yield movement up, you will see a higher cost eventually. And that's partly playing to in this quarter also. We are fully funded on our pension. So we don't have any lag on that. To that extent, it has some impact. But having said that, the incremental requirement for pensioning in the period ahead will start moderating.

Kaushik Poddar: Okay. So this 50%, you're talking last quarter of this financial year, right, cost to income?

Shyam Srinivasan: We are working towards that. It's not last. It's first quarter of FY '25.

Kaushik Poddar: Okay, okay. Thanks.

Shyam Srinivasan: More towards FY '25, yes.

Kaushik Poddar: More towards FY '25. Okay. Means FY '25 as a whole, right? That's what you are speaking of?

Shyam Srinivasan: Yes, yes.

Moderator: The next question is from the line of Jai Mundhra from ICICI Securities.

Jai Mundhra: I have three questions. First is, if you can give the loan mix by benchmark. I mean, Repo, EBLR, fixed rate book?

Shyam Srinivasan: Venkat, do you want to go?

Management: Yes, yes. It's 51% on the EBLR, about 26% is fixed, and if I reflect, 13% is NPLR, which are the big ones. And then we have FX link of 3%, staff 1.5%, and IBPT 1.85%.

Jai Mundhra: Sure. And sir, in this quarter, so the yields on advances have actually changed the trajectory. Earlier, they were moderating for the last 3 quarters. But this quarter, there has been a rise at around 14 basis points. Apart from newer loans, which are high yielding, are you also seeing benefits on either fixed rate book or NCLR or T-bills linked repo, or that benefit is not that much and the benefit is coming from high-yielding book?

Shyam Srinivasan: So high-yielding book is only one element here. There are elements that are across the sector, renegotiations, writing up existing assets, negotiating better price requirements from customers. So I think it's a combination.

Jai Mundhra: Right. Okay. And lastly, sir, on your deposit, right. So you mentioned that deposits are available at a certain rate. So when you intend to grow at 18%, 20% on loans, do you see a scenario where the retail card rates on deposit may have to be increased? Or you think that is an unlikely scenario in the near term?

Shyam Srinivasan: Our philosophy on deposits, we won't lead the price increase. We are tending to be competitive. We benchmark against 5, 6 banks which we compete with. And we won't be off, because I can't have my feet disadvantaged in growth of deposits. As long as we are competitive, we will keep growing, and will get pricing appropriately.

Moderator: We'll have to take that as the last question. I would now like to hand the conference back to Mr. Souvik Roy for closing comments.

Souvik Roy: Thank you. And I want to extend my gratitude to all of you for joining us today, and your interest in the bank and your, of course, insightful questions are greatly appreciated.

So before we close, answer to Rakesh's query, INR35,616 crores, and what we have reported as MSME plus CoB INR31,447 crores, the difference of INR169 crores has been reclassified, which is why it is not a part of BuB or CoB anymore. So which is why you see a 16% Y-o-Y growth, but happy to connect after the call and explain further.

And as we discussed throughout this call, the momentum is strong, and we are committed to further improving our performance. And we firmly believe that the future holds better and great opportunities for us.

If you have additional questions or need any further clarifications, please don't hesitate to reach out to us and we'll certainly answer you. And thanks again for your time and attention. We look forward to our continued journey from here on. Thank you so much. Have a great day.

Shyam Srinivasan: Thank you.

Shalini Warrier: Thank you.

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