"CSB Bank Limited
Q3 FY2024 Earnings Conference Call"

January 29, 2024, 05.30 PM IST

MANAGEMENT : **MR. PRALAY MONDAL**
MANAGING DIRECTOR & CEO - CSB BANK

MR. SATISH GUNDEWAR
CHIEF FINANCIAL OFFICER - CSB BANK

MR. B.K. DIVAKARA
HEAD - STRATEGY & CORPORATE LEGAL - CSB BANK

ANALYST : **MR. SHIVAJI THAPLIYAL**
YES SECURITIES LIMITED

Moderator: Ladies and gentlemen, good day, and welcome to the CSB Bank Q3 FY'24 Earnings Conference Call hosted by YES Securities.

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 this conference, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Shivaji Thapliyal from YES Securities. Thank you, and over to you, sir.

Shivaji Thapliyal: Thank you, Dorwin. Good evening, and a warm welcome to all those who have joined the call. The CSB Bank management is represented by Mr. Pralay Mondal, Managing Director and CEO, Mr. Satish Gundewar, Chief Financial Officer, and Mr. B.K. Divakara, Head Strategy and Corporate Legal. We specifically thank the management of CSB Bank for giving YES Securities the opportunity to host their results call. The management will first be making some opening remarks after which we will throw the floor open for questions. I now invite the management to make their opening remarks. Pralay, over to you.

Pralay Mondal: Thank you, Shivaji and Dorwin. Thank you so much for hosting this call, and thank you all for joining our post results call of Q3 FY'24. To start with, I think globally the high-rate regime has peaked out with many central banks now indicating a pause and a subsequent cut-in rates. The inflation has also moderated significantly despite some uptick last month due to base effect. Geopolitical risks however persist. Prolonged Red Sea blockages could spike the oil prices again. With this, the probability of rate cuts in the next 1 year has come down to 3 from 5 in the U.S., and Eurozone has extended its pause at least till June 2024.

On the domestic side, I think Indian inflation has showed some moderation, though the CPI turned higher to 5.69% from 5.55% in November, though it was slightly better than what was expected. On an average basis, the core and headline numbers are showing moderating trends. This also suggests that the rate hike cycle in India has peaked, and more inclined towards moderation in future. The main concern, however, has been the persistent liquidity deficit in the banking system, which even touched INR3 lakh crores in the recent past. It adds to bank borrowings and deposit cost. We expect the liquidity conditions to improve in FY'24 - 25.

With credit growth outpacing the deposit growth in the banking sector even in this last quarter, the deposit rates are likely to remain elevated in the entire FY'23-24. On CSB numbers, we had a stable Q3 and we could grow faster than the system maintaining a NIM of above 5% on a quarterly and a 9-month basis.

Coming to highlights of our performance, the bank declared a net profit of INR415 crores for the 9-months ended 31/12/23, up by 6% over the corresponding period last year. Q3 FY'24 PAT is at INR150 crores, a 13% increase over Q2 FY'24. Operating profit witnessed a growth of 9% on a 9-month Y-o-Y basis. Q3 FY'24 is up by 12% over Q2 FY'24.

Provisioning buffer of INR 167 crores, over and above the regulatory requirements has been maintained. Despite margins being under pressure for most of the banks in a highly volatile market, we could maintain a NIM of about 5% on both a 9-month basis and a quarterly basis at 5.11% and 5.10%, respectively.

On a sequential basis, cost of deposits increased from 5.22% to 5.42%, while yield on advances improved from 10.88% to 11.49%. Recorded a healthy ROA of 1.78% and 1.84% as on 31/12/23 on a 9-month and quarterly basis annualized, respectively.

On the liability side, deposits grew by around 21% Y-o-Y as against industry growth of 13%. CASA, we had a muted growth relatively at around 6% Y-o-Y, and TD grew by around 27% Y-o-Y.

On the asset side, net advances grew by 23% Y-o-Y. Industry had grown around 16% without the merger impact. Gold portfolio registered a growth of 23% Y-o-Y on a net basis. Portfolio build-up has happened across all sectors. Gold, other retail advances and SME did well in the quarter with a Y-o-Y growth of 23%, 44% and 28%, respectively. On a Y-o-Y 9-month basis, our yield on advances improved by 39 bps to 11.19%.

On the asset quality matrices, Bank had a stable asset quality with GNPA of 1.22%, NNPA 0.31%, PCR of 75% without write-off. We continued with the accelerated loan provisioning policy in excess of RBI requirements.

On the capital side, bank could maintain a CRAR of 22.99%. We have a low proportion of risk-weighted assets compared to the industry, partially because of the higher share of gold loan portfolio in our bank. If you see the shareholder value creation, on a 9-month basis we had an attractive EPS, book value per share, ROA and ROE, which underlines our firm commitment towards the maximization of shareholder value. Book value per share touched INR200. EPS as on 31/12/23 on a 9-month annualized basis is INR 31.78 and we had an ROE of 17.29%.

In conclusion, I would like to say that market is offering ample opportunities for banks to grow their asset book. In order to tap the same, banks have to ensure availability of sufficient liquidity and funds and the tight liquidity conditions prevailing in the market, which is in the deficit mode now is making the job tougher for the banks. Cost of deposits and borrowings is at elevated level. Banks have to carefully manage multiple factors like CD ratio, LCR, NSFR, NIMs, etc. Fortunately, in most of these criteria, we have fared pretty well in this quarter.

Hope by this time, you might have gone through our numbers uploaded on our website. We sincerely believe that we have done exceptionally well under the given circumstances, as we could balance the growth, cost and liquidity aspects especially in a tight liquidity and competitive environment, with most of the ratios showing an improvement. We look forward to doing better in this quarter as well.

Lastly, I want to talk about the additional recognition as the best bank. We got the Best Bank award in the small bank category in the prestigious Mint BFSI awards for 2023.The commencement of CBS migration project is propelling us to resolutely move towards fulfilment of our vision - SBS 2030, wherein we aspire to become one of the most respectable mid-sized bank.

We have just launched our CBS project. We are probably one of the first bank to go for Oracle OFSA OGL altogether in one transition at one go. We'll be leveraging our full service banking license and building a pan-India franchise. We will also be pursuing the branch expansion as a key strategy to fuel the growth.

Our management team is now complete and the entire senior management team has joined, including recent induction in the CRO position, in the treasury position, and also, we have our wholesale banking head, who has just joined us now. With that, we expect that our wholesale, SME, gold and retail, all of that will be the future cylinders of growth of the bank in coming years.

With that, I will open this conference for questions. Thank you very much.

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

Mona Khetan: Congratulations on a good set of numbers. So my first question is on growth. So if I compare versus last quarter, what you gave in your PPT, the segmental loan book, the SME growth has been flattish. So how are you looking at it? How have been the disbursement trends here? And is it more to do with the rundown that you've been alluding to in the portfolio?

Pralay Mondal: Thank you Mona for your question. You asked the growth question, is it? I didn't get the exact question?

Mona Khetan: Yes. I'm trying to understand the growth. So if I look at Q-o-Q, which is last quarter versus this quarter, the SME growth was flattish- growth in the SME book. So I'm just trying to understand because this is your core portfolio, why are you seeing a flattish growth? And if it has to do something with the rundown in the portfolio that you've been alluding to some time back. And if you could give us some color on the disbursements in this book.

Pralay Mondal: Let me answer the growth question first. Yes, I think we had a 23% growth year-on-year on gold. In terms of disbursement, we had a relatively muted quarter on the gold side. There are two, three reasons for that. We just wanted to balance the portfolio a little bit more between gold and non-gold because with this growth also gold is touching 48% of our portfolio. We need a more balanced portfolio.

The second thing is on gold LTV. We have remained focused on gold portfolio with a 74% LTV. When you look at that kind of an LTV, there are many players in the market who are willing to give higher LTV. However, we do not want to get in to higher risk because I still think that though global gold price has come down slightly, still it is at reasonably elevated level. Given that, we don't want to take a higher LTV on gold at this point of time. That's why we are cautious on that side.

Thirdly, we had put lot of improvements in the gold loan process from a system implementation perspective. Because of those kind of implementations, we have slowed down in certain products on the gold loan side, which we would like to continue to do.

The other side of the portfolio, whether it is wholesale, SME, retail, etc, is starting to pick up now gradually. We want to manage the gold loan book as a less risky & more compliant one, and where we should be able to manage the price volatility factor. That is the reason why our gold loan LTV has been reasonably stable, well below 75%.

Coming to your question on SME, I think we have grown by around 28% year-on-year. Quarter-to-quarter, obviously, situation may vary. I'll tell you the issue on both wholesale and SME. You didn't ask me the wholesale, but let me also say that wholesale also slowed down a little bit.

The cost of funding is going up in the system. Given our NIM objective, we actually did not want to do businesses, which would be very competitive in terms of interest rate because then interest rates will be lesser. SME loans are generally linked to repo and 6 months down the line, 7 months down the line, who knows when interest rate starts falling again.

When it is linked to repo rate, immediately when the repo rate falls, we have to reprice the SME portfolio. Given the liquidity challenges on the liability side and with still the repricing on fixed deposits going up, the cost of funds has not seen the peak yet. It may continue to go up a little bit more. Given that, we wanted to do business only what makes sense for us from a NIM and a profitability perspective. That's why you will see that both on the SME book as well as on the wholesale book, we had not done few businesses which would have otherwise picked up. The old SME book has been running off, as it normally does.

We had some run off of say 10-20 Crs on the old MSME book this quarter. Given that perspective, I think overall, the growth is relatively muted. This is also deliberate. All this contributed towards a 23% growth year-on-year for the bank, vis-a-vis what we do generally; say around 27% - 28%.

This also has helped us in maintaining a CD ratio of below 83%. Last quarter, the CD ratio was above 87%. Our LCR for period end is 123% and average is 113%. All these decisions helped us in managing a more balanced growth with an eye on how the funding cost is going to go up and how the linked books will have a challenge in terms of maintaining earnings. That is broadly how we took a prudent decision both on wholesale as well as on SME businesses.

Mona Khetan: Got that. That's very clear. Just one small aspect on growth. So within other retail, I just want to understand what is driving growth? Is it mostly secured asset?

Pralay Mondal: In retail?

Mona Khetan: Yes, when we look at other retail.

Pralay Mondal: Yes. I think two, three products are doing very well for us. One is the auto loan. Inventory funding is also doing well for us. Commercial Vehicles (CV) and Commercial Equipment's (CE) is doing well for us. LAP is doing well for us. These are the three four products which are doing well for us.

Credit cards that is on a zero base, is also doing well on a year-on-year basis. We started credit cards in alliance with two partners. While we had grown the unsecured business till Q2 of this year, we have significantly slowed down this quarter based on whatever we are hearing in the market.

We have almost slowed down our unsecured business growth, not because of any issue in the portfolio, but because what we are hearing in the ecosystem. It is too nascent a portfolio to have any problems.

Mona Khetan: Got that. So my second question is on the deposits. So you had earlier alluded to your comfort level with around 90% of CD ratio on the peak side. And we have this quarter seen a sharp decline in CD ratio. So would that comfort zone come down here on because we be hearing a lot that RBI has been guiding banks to lower their CD ratio level. So what's your take on that?

Pralay Mondal: We have to look at many ratios, just not CD ratio. On the CD ratio, we looked at two major aspects. One is the incremental CD ratio. That is where it went below our comfort level. So, I said that, we will bring down the incremental CD ratio, which automatically will bring the CD ratio down.

Secondly, I said 90% is a comfort zone in a comfortable environment when business is usual, and everything is fine. But that may not be right when you have a INR3 lakh crores liquidity deficit. I am a very risk averse person. Given that perspective, in that environment, relatively on a small balance sheet like this, these percentages can swing big time this way, that way in a very short span of time.

I would like to err on the side of caution, where it impacts my NIM. All this surplus money, will go into investments, which has resulted in negative yield right now on an incremental basis, whereas your funding cost is higher than that.

I still say that liquidity risk is also a risk in the system. Given the situation, what it is, how do we know what happens next year. Given that, I think we took a conscious call saying that let's wait and watch for a while. It's not that we targeted 83%. It is just that we said that we don't want to do business below a certain rate and with a certain kind of a risk.

So once we stop doing that, automatically, we reached a level of 83% on CD ratio. Is it that we can go up to 85%, 86%? Answer is yes. However, to ensure that we do not touch 90%, we need to apply this caution, so we have applied this caution at right time.

Mona Khetan: Got it, sir. And on the cost of fund side, so when do you see it peaking? Could it easily comfortably go up for the next two quarters as well, given the liquidity environment?

Pralay Mondal: Yes. what will happen Mona is, it completely depends on the tenor of deposit portfolio. Typically, people who were sitting on a longer tenor, when the interest rates started going up, the deposits will come for repricing now. For people who are sitting on a short-term tenor, the repricing has already happened. So it depends on that situation, which bank is where.

Most of our deposits are typically around 1 year. We do not have very long tenor FDs right now. I would say that give it another 3 months, it will be a sort of peak. However, what we do not know is whether this liquidity challenge is over, because the problem is the incremental business. I thought this quarter it has peaked. However, until the end of the quarter, I saw CD rates in the market, especially on the shorter term - which is 12 months and below, at elevated levels. Given that perspective, it is very difficult to say that how the cost of funds will go. We are factoring in a situation where next 3 to 6 months, it can still go up. But for us, the deposit repricing reason - I think that will be over in the next 3 months.

Mona Khetan: Sure, sir. Got that. And just one final question on the credit cost front, so we continue to see negative credit costs for the bank for the last couple of quarters. So is this mostly driven by recovery from written-off accounts? And how big is the written-off pool as of now for the bank?

Pralay Mondal: That data may not be in the public domain, but I'll give you a sense of flavour to your question. We have been on a negative credit cost for a while now. But will it continue forever? Answer is no. Next year, it may not continue at this level. But even if you look at this quarter, let's look at each of the parameters. The slippages are significantly lower than last quarter's.

The GNPA is lower. The NNPA is lower. Recovery is also slightly lower than last quarter, but still it is relatively ok.

Given all this, we are at INR 106 crores of contingency provision, plus another almost INR 61 crores of provision because of our conservative provision norm. Overall, INR 167 crores of overall additional provision, is there in the bankbooks. Not that we want to touch this contingency provision unless it is as per formula what we have decided. To that extent, we are really sitting on a very safe quality portfolio though negative credit costs may not continue forever. But given that slippage is low, I think that is more important to me than recovery-based negative credit costs. That itself is very comfortable. So on this front; I think we are doing very well.

Moderator: We have the next question from the line of Manan Tijoriwala from ICICI Prudential Asset Management. Please go ahead.

Manan Tijoriwala: I just had one question. Sir, I see the yields have improved almost 68-70 bps quarter-on-quarter. So could you walk us through what exactly has changed from last quarter because last quarter, we had some gold loans issues which we pegged down, so that profit came down. So how does it come back now?

Pralay Mondal: Thanks for your question. So two things have happened, Manan. One is, as I said that we took a very conscious call of not doing businesses, which will come at a low yield. Because, I looked at it this way - what is my incremental cost of deposits? If I take that incremental business; on an incremental basis, why do & how I need to take that business on the SME side or on the corporate side, which I just explained to Mona. So those businesses we refused. I said that we'll not do businesses on averages. We'll do business on marginal costing vis a vis marginal additions. That's the way we actually very consciously improved our yield.

On gold loan also, if you see that last quarter, we ran off some of this book. We have started rebooking some of these businesses now because our LTV has now come down to a level where we wanted it to. So given that perspective, we could start booking gold loan at a higher yield again, because our LTV is at a comfortable level. But again, if we see our LTV going up to 78%, 79%, 80% not because of our reasons, but because of market reasons, which is price driven, say gold prices falls, then again, our yield will start coming down. Because then again, we will slow down some of this portfolio which will come at high yield and a higher LTV.

That is the reason why this will be seasonal to some extent and will vary based on the gold prices. But primary reason for yield increase is basically we refuse businesses which are coming at very low yield and very competitive yield. We said that at our marginal cost of deposits, this is not making sense.

Manan Tijoriwala: But it's largely from the gold business, and if I understand correctly, the increase that we're seeing now.

Pralay Mondal: Our yields have gone up in retail viz Agri, MFI, gold etc. Overall yield also has gone up, thus creating a good story for us.

Manan Tijoriwala: Understood. Sir, one more question on the CASA plus retail TD, how is the performance going? And how do you see it from here on? As in if you could see -- if you could talk about what it was, say the same time last year versus this year now?

Pralay Mondal: We have grown CASA by 6%, I've told it in the past also that it will take us at least 1 more year to start building the CASA franchise. Because primarily, we have been a gold loan franchise and most of our customers have not been in that level where you can build a very strong CASA franchise.

While all other things are in place, like the branches, the distribution, the people, the leadership, the products etc, unless we have the system, I am not willing to invest. After acquiring so many customers where we cannot give the kind of a service, which HDFC or ICICI or Axis can give, then it will be difficult to build that franchise.

So I'm keeping the franchise growth on my CASA, including CA only after FY'25 onwards. Until then we will depend to some extent on the retail TD. It's not that CASA is not growing. CASA is growing, but only at a certain level. And that's the story of the industry also, they are growing slow, but we are growing slower. We are saying that we will build deposit franchise from FY'25 onwards.

Till then to ensure that we support our growth, we'll have a funding structure in place. Now the funding structure will be a combination of CASA – which will be a small portion of that, and we'll retain our growth of anywhere between 5% to 15%. So the CASA percentage is not going to come up too much, if you continue to grow at 20%, 21% on the deposit side.

But what will happen is that we are looking at other borrowings as another way. Our CD book is also doing well. We have built slightly larger deposits, based on our relationship. We have created a vertical on TASC. While we are growing the retail deposits, but at the same time, we are building from the other sources as well.

This will continue for another year or so, and then we will start building the liability franchise. I am being very honest about it right now. There's no point talking too much about the CASA and retail franchise till our systems and processes are in place. Once that will be in place, we have completely planned it out from FY'25 onwards.

Moderator: The next question is from the line of Prabal from AMBIT. Please go ahead.

Prabal: Sir, my first question is again on the deposit side, so congratulations on the kind of accretion mobilization that we saw during the quarter. In term deposits are there particular schemes, say, 190 day schemes or 500 day schemes, which is helping up beef up the mobilization?

Pralay Mondal: Yes. Almost every bank has, we also have a particular bucket. Typically, most of the deposits gravitate towards that bucket - 401 days is our bucket where we get 7.75%. Most of the 1-year plus kind of a deposit is coming in that bucket.

Having said that, there are deposits which also comes at a slightly more elevated costs also closer to 8%. Those are typically slightly larger ticket deposits, typical institutional deposits, etc. Also, we have to understand that in such a way the entire design has happened between LCR, NSFR, CASA ratio, deposit growth and CD ratio, the whole complexity is such that there is no escape of doing one kind of a business - you have to have a very balanced business model.

I must give credit to the team, that the way they have built up the entire business where we have ticked almost all the boxes. Deposit growth, we have ticked. LCR, we have ticked. CD ratio, we have ticked. Only we have not ticked the CASA ratio, and I'm telling you this will not get ticked for the next 2 years. Cost of funds, we have ticked. Almost all the parameters we have ticked. So there must be something which we are doing right on the liability side of the business, in spite of the fact that we are not having our franchise, which will happen FY'25 onwards.

Prabal: Understood, sir. Sir, my second question will be, going ahead, the cost of funds rise for us which is true for the system as well. Which are the segments of the loan side where we can pass on these higher cost of funds? Because gold loans typically are quite volatile, they tend to be in the range of 11% to 11.5%. So are there some other segments that you've identified where you can pass on these rates?

Pralay Mondal: Yes. Cost of funds has typically gone up by around 1% or so in the last 1 year on a 9 months basis, cost of deposits have almost gone up by 1.1% on YoY basis. So roughly, anything between 90 basis points to 130 basis points depending on what kind of cost of funds/deposits we are talking about has gone up.

How do we pass it on? Answer is some we cannot. That's why you see that our NIM in spite of the fact it is 5.11%, last year on a 9-month basis it was at 5.52%. 40 basis points sacrifice on

NIM has already happened on a 9-month basis. We cannot pass on everything. Having said that, I think if every business starts picking up a little bit, there will be a change.

The way I handle it on the execution side, it is very simple, I tell wholesale that if you were at this level, you have to get me 20 basis points more. Same thing I tell SME. SME has actually given me a much higher yield this quarter; so has the gold loan portfolio

I think it's that incremental part, which is more of an execution story, it's not that one size fits all. But yes, there is some impact on the NIM, which you can already see when you look at a year-on-year basis, roughly around 40 to 50 basis points impact on the NIM.

Prabal: So let's say, 20 basis points higher on some segments. This is driven by more prudent or selective customer basis? Or how do they how -- how are they able generate more yields from same portfolio?

Pralay Mondal: It's very simple. I said that below this yield, we would not do business. In fact, when I look at data of other banks, the variation of yield between 1 portfolio or 1 customer to another portfolio and another customer is anywhere between 6%, to 8%.

For us, the highest yield is around 12%, lowest yield is around 8.7% or 8.9% or something like that. Our range is very low, between 3% - 3.5%. That's the way we operate in a very small range. So what it means is, effectively, we are not taking the high risk. We are willing to sacrifice business, where we think that the business ROA is not right for our kind of a bank at this stage.

Some of the other banks can do it because they have other incomes, whether it's on the wealth side, whether in the transaction banking side. I'm not saying they're doing wrong business, they're doing the right business. But given the life cycle we are in right now, because our cross-sell opportunity into wholesale and SME is relatively smaller compared to some of these other large banks, so we have to primarily play the yield game.

We play in this 9% to 12% range. 12% for gold loans. Actually less than 12% here and more than 9% there. So in that range, we operate. We refuse business which doesn't make sense for us. But that does not mean we're taking higher risky business.

Prabal: So let's say, if the maximum is 20%, and with our opex...

Pralay Mondal: There are some agri business, which can be slightly higher than that, some micro finance, which can be slightly higher than that, but they are small in terms of contribution to the portfolio. I'm taking out the agri and the microfinance business, but they are very small in terms of contribution to the bank.

Prabal: But we see the cost of funds of 5.5% and Opex to asset of 4%. If you are doing business at say 11%, that is hardly making us money in an environment where credit cost is benign, this could still be supportive to us. But as the environment normalizes, could there be a risk of ROA or return ratios getting diluted because of this strategy?

Pralay Mondal: Let me put it this way. The way you're calculating then banking business would appear not to make any money. I can put our calculation and say that in spite of all this, I'm having a NIM of 5.11%. So it depends on which statistics you're looking at.

Plus, when you look at ROA, we have almost 1.8% ROA, which also happens because now on the non interest income to total income, we have now almost 14% on consistent basis. This was below 5% at some point of time in the bank.

So how you create the ROA tree overall and how you ensure that you manage the cost of funds and build the right business depending on what ROA you generate. I don't think that calculation works for us, because there will be businesses which also comes with lesser risk weights.

There will be businesses which comes with a lot more franchise building on the wholesale side in the long run. Some of these are funded with lower tenure kind of deposits from ALM perspective. It's more complicated than this. But net-net, we are saying that our NIM will be 5% for the full year or more.

Next year, even if it comes down a little bit, it will not go below 4.5% under any circumstance. ROA, we will be between 1.8 to 2%. Next year, we will be even in a difficult phase, where our other businesses are picking up, where ROA is lesser; we will be within 1.5 to 1.8%. Given that, I think that's the game we'll play, and we should be able to deliver that.

Prabal: Sir, just last one question. So you mentioned about balancing growth between gold loan portfolio and non-gold loan portfolio. So which sort of segments this quarter we can see retail picking up by 5% sequentially? Going ahead, which segments would you say that are ready for now growth traction and we should start seeing pickup there as well?

Pralay Mondal: See, for another 2 years, we are in love with gold. Gold will continue to do well because it doesn't need risk weights much. It has high yield. Our loan losses are minimal. The NPA in gold loan is lesser than the bank level NNPA, which itself is only 31 basis points. Gold loan NPA is lesser than that and the cost of operations is high, but that is already baked into the system.

As long as these equations are there, we'll continue to focus on gold loan and do those business. I said in the long run by FY'30 gold loan will come down to 20-odd percent, not because we will de-focus on gold loan, but because all other businesses will start picking up after system starts delivering, which will start from FY'25 onwards.

Having said that, to your question as to other than gold loan, which other portfolios will start doing well., this year was muted in wholesale. I think FY'25 onwards, our wholesale will start picking up, SME will significantly pick up. Already SME is showing a 28% YoY growth this year for the first time in a long period. I think they are fully engaged to take the growth further.

Retail on a small base, will grow much faster, but will it materially contribute? The answer may be no because ultimately, it is only 15% including Agri/MFI and 9% on a standalone basis. Some of the businesses which we did not do so well, like Agri, MFI this year, will start picking up next year.

Overall, I think we should be able to grow. Growth in assets is not a problem for us. Our constraint will be, can we grow liability at more than 20% consistently with a reasonable cost. So that is something we have to notice. If we are able to grow that, then we have to choose which one we want to grow. Therefore, constraint is liability; not growth on the asset side.

Moderator: The next question is from the line of Pallavi Deshpande from Sameeksha Capital. Please go ahead.

Pallavi Deshpande: Just two here. Just first one would be what would be the increase in the rates that we've passed on to the NBFC given the increase in the risk weightage? And second question would be on the retail loan side, what share of the book is unsecured which you referred to which slowed down this quarter?

Pralay Mondal: What is the second question, unsecured?

Pallavi Deshpande: What is the share of unsecured loans to the total book?

Pralay Mondal: On the first question, let me tell you that - yes, RBI did raise 25 basis points on NBFC risk weights. However, we have not passed it on as such, unless there is a renewal happening. Because my thinking is like this. If there is a risk somewhere, why take higher risk.

We have got little more cautious and seeing which are the kind of NBFCs, because it is a translated risk. Hypothetically, if there is a risk that is emerging in unsecured space and small ticket unsecured space, and if certain NBFCs are doing business there in a large amount, then if we lend there, then it's a translated risk, which is coming back to us. That's the challenge.

We have started getting lot more careful on this kind of NBFCs where this kind of businesses are happening. We have refused many of these businesses this quarter. So we have taken it more from a risk guidance perspective than a yield maximization perspective.

Secondly, going ahead, I think while our NBFC proportion is slightly high in our wholesale book, but we have taken a conscious call of actually growing the other portfolios, which will automatically bring down the NBFC as a part of the book. That's the way we are going to manage this. We are taking the RBI direction, not as a yield maximization but as a risk management tool. On the second question on unsecured to total? What is it, Satish?

Satish Gundewar: Pallavi, we don't have this information in the public domain in terms of what is the total unsecured. But if you look at the overall book composition, 48% is the gold loan, which is anyway fully secured. Then within retail also, quite a few products which we are doing are secured like CV/CE and all. Even SME also, it was secured business. It is a very small kind of a percentage

Pralay Mondal: So Pallavi, I'll tell you a simple answer. Our unsecured retail book in the whole bank is around 5 %.

Moderator: The next question is from the line of Shivaji Thapliyal from YES Securities. Please go ahead.

Shivaji Thapliyal: Yes. my question is really regarding having some more color on the SME -- broader SME segment. So just, wanted to understand what are the sub segments within SME? In addition, what are the ticket sizes and what is the yield maybe for those sub segments? And between these sub segments, would -- are you getting the sense as you are piloting initiatives that maybe one segment is more attractive for you to do at this point in time over the next couple of years.

Just some color around what is happening within the SME segment. And also on the retail side, while you have answered which are the segments that you are seeing traction, but maybe from a long-term perspective, what will be some of your bread and butter retail segment? Will it be affordable housing, which part of vehicle finance and some color on the sub segments within SME and retail would be helpful.

Pralay Mondal: Thanks, Shivaji, for both the questions. Both are very critical questions. Let me answer the retail first, then I will invite our Head of SME, Shyam Mani to give you full color of the SME business that he's building. On the retail side, again, because you said long term, I will divide into short, medium and long.

Long term, our retail verticals will look at building the portfolio exactly the way the industry does it; home loans, personal loans, auto loans, credit cards, all of that in a similar kind of a proportion. Fundamentally the way we'll build our retail portfolio is based on how our liability franchise is getting built, which means how a customer getting acquired, cross-selling is done and so on. We are not going to go out and buy retail business through DSAs and all this external kind of channels.

If that does not happen, our retail book will mirror how the customer franchise is building and based on this, cross-sell to them. This is how I had built businesses always. This is how we'll build it here. In the short term, till the liability franchise starts picking up, which will take 1 or 2 years till then we are doing businesses primarily through our internal customers. We are building bridge with the manufacturers, with the end customers directly etc. Hence, short term is mirroring those kinds of products like our auto, commercial equipment, commercial vehicles, loan against properties, health care business etc. These are very niche businesses direct to customers, and you can address this segment in a wholesome manner because these are not distributed segments.

These are very concentrated segments, so we can address these customers and with our value-added services, with the manufacturer tie ups etc, we can do these businesses. That's primarily where our focus is in the short term is. But medium to long term, we'll be exactly mirroring the franchise we will build on the liability side of the business.

That's the way we'll do retail asset business, the typical and classical way of building that business. On the SME side, you talked about the yield and all that. On the yield, I think we are somewhere between 10% to 11% in SME book. Rest of the things segmentation and all, let Shyam answer this.

Shyam Chandher Mani: Thank you, Pralay. Just want to give an overall brief in terms of the way we have started scaling up on SME business. If I look at purely on a top line growth, volume of disbursement, both fund-based and non-fund based put together, we have grown 108 percentage as we speak.

Net growth is what it's hovering around 28 percentage YoY at this point of time. Of course, there's been a late pickup because we were working on setting up our process, systems and the platforms right and also in giving effect to some of the policy upgradations which were required. Post that, we are starting to see a momentum in the business. If I have to compare FY'23, we had ended up at around 4 percentage, currently it has moved up to 28%. So this time, quarter-on-quarter, there is an upside movement of about 5%, in the overall net SME book as well.

This year, as we speak, on a fund-based book alone, an overall disbursement/limit setting of around INR1,066 crores has been done. Both non fund-based and fund-based put together it is INR1,456 crores. So that obviously talks about the growth momentum. We had to let go of some clients due to interest rate pressure/ stress signals etc

As Pralay was mentioning that we're not compromising on the yield, and that's why overall the momentum and the yield were in line with our expectation. Specifically, on the ticket size, which you asked, the new-to-bank ticket size is around INR 6 crores, and overall ticket size at the portfolio level will be around INR 2 crores to INR 3 crores.

We follow a branch centric hub-spoke model, where SME clusters and the key branches are identified and thus we focus on the top 42 branches. Within that, we focus on top 20 branches as catalyst and the next 22 branches as prime branches. And around that, we work with trade bodies, industries, associations etc in terms of engaging with them so that we go and reach out to them with an industry solution.

We had certain knowledge banking advisory tie-ups as well so that there could be a value add to these associations and industries. Primarily, the focus sector for us is manufacturing. Within manufacturing, light engineering as well as automobile, health care, pharma, food processing and to some extent, textiles and apparels. And that's the way the progress has been, and we're very positive about further growth on this.

Shivaji Thapliyal: My next question was around operating expenses. So I mean, while you have given an ultra long-term guidance that cost-to-income ratio will decline several years later. But -- just how -- what is the composition of the cost at this point in time? I mean, how much of that may be technology investments and for how long will these technology investments kind of continue? And when will they start to taper off? What -- so just some understanding of the glide path when it comes to operating expenses would be helpful.

Pralay Mondal: Yes. There are 3 primary costs if you look at the cost line. One is people. One is infrastructure/distribution and the third one is technology. These are the 3 primary cost lines for us. Within that, as you rightly said, technology is highly front-end investments because we are rebuilding and rebooting the bank from an infrastructure perspective, technology as well as other infrastructure.

However, a lot of this is capex. So it will flow through the P&L over the next 4, 5 years. But most of these investments will be done in the next 2 years. Then only MCS and some add-ons here and there will keep happening, which are like opex post 2 or 3 years. It will go through for the next 4 or 5 years, but it will start tapering off maybe by FY'27, '28 onwards, and then it's a two-year payback for technology starting from FY'27, '28 onwards and hence, the cost to income ratio will severely taper off to below 50% by FY'30

Coming to the next, which is distribution cost, typically, we will add around 75 to 100 branches every year, which as a percentage will be going down as the branches start picking up. On the manpower side, that cost will keep growing because we want to keep investing on the acquisition side because once we have the technology ready for building the retail franchise, our manpower costs will continue to elevate, but not at the same level.

We have an increase of somewhere around 30% in manpower costs. That will start tapering off in 2, 3 years because as the wholesale starts picking up and the SME starts picking up, then on a cost-to-income basis, it will be lower as those are low cost-to-income businesses. Once that mix starts going up and revenue starts coming from there, then cost to income also starts tapering off.

Also on branches, not only percentage of new branches will start coming down, some of these branches we are investing will also start breaking even within 2 to 3 years of setting up, and that also will start tapering off.

We have done all these calculation, and that's where we are saying how confident we are that by FY'30, our cost to income will be well below 50%. Currently for the next 1, 1.5 years, it will remain around 65-odd percent or close to it. Then it will start tapering off maybe by FY'25, '26 onwards below 60% and then below 50% by FY'30.

Moderator: We have the next question from the line of Pallavi Deshpande from Sameeksha Capital. Please go ahead.

Pallavi Deshpande: So just wanted to understand again on the previous, the cost to income side. Like you mentioned, we have this -- where does it peak, I mean up or are we exclusively implementing now. So that is implemented by when? And 65 is the peak or do you see it going beyond that in the short term?

Pralay Mondal: CIR is hovering between 60 to 65% right now. We were very close to 65% a quarter or two back. Now we are back to somewhere around 62%. But this will keep happening because of other income or cost because it's a ratio at the end of the day. In the short term it will be hovering between 60% to 65%.

But for sure, it will start on a glide path starting from FY'25, '26 onwards. And then it will go to below 60% and then below 50% by FY'30, that's what I said. But right now, it will fluctuate a little bit because it will vary in terms of income and costs and things like that. But for sure, the technology costs will be hitting us for the next 2 years.

Pallavi Deshpande: The tech spend would do will be what percentage of PBT number, I think for the large bank, it's around 9%, 10%, perhaps you could...

Pralay Mondal: It will be well above that.

Pallavi Deshpande: Right. On the income side, you can have other income and the absolute amount, or do you have some guidance, right, the increase in absolute amount for the mix.

Pralay Mondal: We know that number, but we don't give it in public domain, but it's a significantly higher percentage compared to what you just mentioned for the next 2 or 3 years.

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

Mona Khetan: Yes. I just had one query on the fee income side. So we have seen a strong growth on the fee side in the last few quarters. But I just want to check whether we still have more levers? Are we already seeing a good contribution from lines like transaction banking or that's yet to play out for the bank?

Pralay Mondal: Very good question, Mona. The transaction banking vertical, we have just started. The TFX income will continue to grow as our wholesale and the SME side of the businesses starts doing the sophisticated conversations with customers, and that will happen now.

Thus transaction banking fee will start going up from next year. We have set up the team. In terms of percentage, you will see that we are hovering between 13% to 15%. Last quarter was exception. But generally, we will be happy with this range because most of the other banks are in this range, except for some large banks who are in the 17% range.

This is where our sweet spot is -around 15%. We were actually at 5% in the recent past. From there, once we reached there, the easy job is done. Now how do we go from 14 to 17 on a consistent basis is the next journey. We'll be happy to be there. I think we'll achieve that also at some stage. But also, you must understand that NII is also a little muted.

Because of that, the ratio is sometimes very high. The ratio is a very funny subject. So now NII also starts picking up, if noninterest income also goes up, interest income goes up, our overall income goes up, so that is fine. But generally, our sweet spot is between 13% to 17%.

Moderator: We have the next question from the line of Shivaji Thapliyal from YES Securities. Please go ahead.

Shivaji Thapliyal: Just one clarification. You pointed out that the tech spend is more than the figure that was quoted by one of the previous participants. So the 9% figure that was quoted is to be taken as a proportion of total Opex or PBT, I mean...

Pralay Mondal: I thought you said PBT

Satish Gundewar: Yes, PBT.

Shivaji Thapliyal: So it's more than 9% of PBT. So how much will it -- so it may not be more than 9% of total opex or what would you peg it at as?

Pralay Mondal: I only responded Shivaji to the question which was asked that some of the other large banks are around 9% of PBT. What I'm saying is that ours is higher than that at this point of time. It may not be forever, but at least for the next 2, 3 years.

Shivaji Thapliyal: Yes. But just to clarify, I think the 9% figure is the ballpark that we have been noticing in other conference calls is as a proportion of total opex and not for PBT.

Pralay Mondal: But I calculate it as a PBT, so it will be higher than the PBT. On the total opex, what is our opex, Satish?

Satish Gundewar: INR312 crores for the quarter.

Pralay Mondal: Then it will be much higher than that

Shivaji Thapliyal: So it's much higher than 9% of total opex.

Pralay Mondal: Absolutely. And this is for the quarter or for the year?

Satish Gundewar: No, this is for the quarter I'm saying.

Pralay Mondal: Then it will not be. It will be around that number, close to that number. Because when I reacted, I thought it is talking about the PBT. If it is Opex, then our ballpark will be roughly 9% of Opex

Moderator: We have no further questions. I would now like to hand the conference over to the management for closing comments. Over to you, sir.

Pralay Mondal: Thank you, Shivaji. Thank you, everybody, for participating in our conference call, and look forward to even more exciting Q4. Thank you very much.

Moderator: Thank you. On behalf of YES Securities, that concludes this conference. Thank you all for joining us. You may now disconnect your lines.