"Federal Bank Q3 FY18 Earnings Conference Call"

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MANAGEMENT: **MR. SHYAM SRINIVASAN – MD & CEO, FEDERAL BANK**
MR. ASHUTOSH KHAJURIA – EXECUTIVE DIRECTOR & CFO, FEDERAL BANK
MR. GANESH SANKARAN – EXECUTIVE DIRECTOR, FEDERAL BANK
MS. SHALINI WARRIER – CHIEF OPERATING OFFICER, FEDERAL BANK
MR. RAJANARAYANAN N – HEAD OF INVESTOR RELATIONS, FEDERAL BANK

Moderator: Ladies and gentlemen, good day and welcome to the Federal Bank Q3 FY18 Earnings Conference Call. 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 would now like to hand the conference over to Mr. Rajanarayanan. N – Investor Relations, Head, Federal Bank. Thank you and over to you, sir.

Rajanarayanan N: Thanks, Stanford. Good evening to all of you and welcome to the Q3 Earnings Call of Federal Bank. The management team here is represented by Mr. Shyam Srinivasan – MD & CEO; Mr. Ashutosh Khajuria – Executive Director & CFO; Mr. Ganesh Sankaran – Executive Director; Ms. Shalini Warrier – Chief Operating Officer; Mr. Sumit Kakkar – Chief Credit officer; Mr. Krishnakumar K – Head of Finance & Accounts and other executives. Over to Mr. Shyam Srinivasan.

Shyam Srinivasan: Good afternoon and thank you for dialing in the first call of the year, so Happy 2018 to everybody. Quick update. Results were approved about an hour ago or so and we have uploaded the results on the website, the investor deck also. So many of you may have had a chance to look at it. Let me just give only the sort of principal highlights and then will as usual take Q&A from everybody.

The important part of Q3 is the momentum is strong on the operating side, continues to be robust both on the credit growth, importantly diversified across all our product segments. Interest income was the highest ever, recorded in the history of the bank, 950 crores was net interest income.

Some of the other milestones; we crossed 100,000 crores in deposits. Our overall credit market share continues to grow quite well. We think we are North of 1.05, 1.07 in sort of market share. Products like Home Loan, Personal Loan, Auto Loan which have traditionally been our lower single digit growth have now handsome growth of high double digit and in particular products like PL and auto loan albeit on a very small base are growing almost 3 digits. Our relationship management structure which we have been sort of strengthening across many quarters is now 330 people plus strong and visible results are as we can see growth across the different verticals whether it is corporate, SME, business banking or retail led by both RMs and the branches. The distribution of business between branches and RMs is now visible. RMs were a much smaller share. Now, it is almost 70:30. So both on a growing denominator, both are growing and which has been the focus of the bank. As you know, we sort of went into a branch light distribution heavy model and that meant virtually freezing on branch expansion for almost 3 years, but expanding our distribution be it our RMs, salesforce, Fedfina and any other opportunity using BCs and Digital. All of that is trending well. We put out some numbers in terms of the digital trend lines also. New account opening both for credit and deposits is gathering momentum. So all in all, the operating performance for the franchise is strengthening. In fact, operating profit for this quarter back out trading gains for the immediate quarter that went by or a similar period last year, operating profit was up 35%. So the underlying momentum is quite strong and we believe that should continue.

The one area that we saw an impact which was certainly on account of trading gains being very lower than either the sequentially previous quarter or the same time last year, but that is well documented. I am not stressing more on that. We had identified a pool of education loan accounts in Kerala which had got some dispensation. Even last quarter, we had signaled that they were under stress and state government had probably signaled that they would give some kind of relief to these customers that had not yet come through, the deadline is 31st January, but we took the entire hit in Q3. So to that extent, the slippages were inflated by 71 crores which is largely the education loan impact. Retail without education loan has shown marked improvement at about 79 crores versus 100 plus in the previous quarter.

So on balance, we think the underlying franchise performance is strengthening. Our RM model is working. The strategy of branch-light distribution-heavy is beginning to gain ground. Distribution and digital are working quite well together and there is momentum. The interest income like I pointed out is an all-time high. We had exceptionally good recovery and upgrade this quarter which did help the overall managing the provisioning and the financial impact of higher slippages that were on account of this education loans that I pointed out. So our credit costs were 59 basis points this quarter compared to 71 the previous quarter. So on balance, the quarter turns out barring the impact of trading gains very much on track and we believe this momentum will continue as we go into FY19, but importantly we have the milestones to cross in FY18 March. Many of them are sort of self-imposed both in balance sheet targets and momentum targets that we have set for ourselves. But the team is confident that those are very much within our reach to deliver. The only thing that we are guarded and watching out for is the migration of the accounts that had either been restructured or sold to ARCs because sale to ARCs, the effect is the same because if there is a degradation on their performance, the provisioning is the same as what it would have been if it is on our books. So resolution is the important part. Recognition of NPAs have all fully happened. So we think the resolution will happen between Q4 of this quarter and next year first quarter. So those are headline points.

We can open it up for questions and answers. Like Raj mentioned, the entire senior team is here, but I will try most of it and ask our senior team to step in as and when it is required. So, go ahead please.

Moderator: Thank you very much sir. Ladies and gentlemen, we will now begin with the question and answer session. We take the first question from the line of Nagraj Chandrasekar from Laburnum Capital. Please go ahead.

Nagraj Chandrasekar: Two questions. First, could you give us a little bit more color on exactly what went wrong with the education accounts. What was the call we took in hindsight, what were the factors we did not anticipate that caused these loans to slip-in, does that in anyway change the way we are looking at this category of loans or overall our retail credit policy? And the second is corporate slippages were also a bit higher than last quarter. So to the extent if you could give us some color on what is driving those in this quarter whether it is just fairly granular slippages or whether there is anything particularly lumpy in that, that will be very helpful.

Shyam Srinivasan: Sure. Let me take the corporate one first. The 98 crores is literally 3 accounts of between 30 and 35 crores each. So there is really no lumpy account or anything that sort of any worry for us on that count and that may continue into the quarters ahead. There will always be one or two accounts 30-40 crores. So we have factored for that between 50 and 70 crores. This quarter, it was three but one of them is recoverable, but yes there is a great chance that it will come back between today and tomorrow, but as of recognition date, they have not served their dues.

Nagraj Chandrasekar: So you may see that last quarter was slightly abnormally low and next several quarters, we should assume somewhere in the 300 range.

Shyam Srinivasan: In corporate or mid-market is never really, there is no trend line to say it will be this, but if you take a 8 quarter period, we have been seeing roughly between 50 and 70 crores in corporate. I am talking of 8-quarter average. So you could argue that in the next 2-3 quarters, this may be the kind of run rate. Upon education loans, the breakup, let me just give you the education loan backup. If you see that is why in our deck also we have put 5 quarters education loan, traditionally has been 7-8-10 crores and some quarter even lower at 2-3 crores and that is the normal run rate. In the beginning of July of 17, the state government came out with some kind of concession so to say which encouraged even bona fide people who are serving their dues to look for some subsidy and therefore everybody is now tempted to go out and see if they can get the state government subsidy and therefore they have stopped even the guys who are paying are not paying. So our overall education loan book is roughly about 800 crores and most of it is in Kerala. We have not grown that book for a long time except where it is a mandatory growth. So this 70 crores is some kind of a reflection of that kind of behavior influenced by some kind of event that the state government encouraged. We had seen this problem coming for two quarters. Last quarter, we made a provision for it, that is why you did not see a large provision impact of that in this quarter. So we upfronted it in this quarter because we said we do not want to drag this along long side. For example, Q4, this will come down to a single digit number. And Just to complete the question, you had said does it have any retail credit policy. We see each of our retail products differently in the policy and underwriting standards and the underwriting mechanism varies. It is sort of fit for purpose. Education loan wherever it is below 4 lakhs and it is mandatory, this is a challenge.

Ashutosh Khajuria: And then the dates got extended from 31st October to 31st December. 31st December, first and from 31st December to 31st January. Had it been only up to 31st December, there has been more resolution, but that is further extended by one month.

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

Jai Mundhra: Sir just again on this corporate slippages of 98 crores, what is the status of this RBI risk based supervision for our bank sir?

Shyam Srinivasan: The supervision is over, but the report has not come out. We do not see anything dramatically altering the picture. The slippage run rates will be similar what you saw this quarter.

Jai Mundhra: Sure and there was no this non-fund based to fund based evolvement in this quarter of this three corporate accounts?

Shyam Srinivasan: No.

Jai Mundhra: Secondly sir, in terms of provisioning, can you give the breakup for loan loss provisioning and investment depreciation for this quarter and how are we placed on the AFS portfolio?

Shyam Srinivasan: The loan loss provisioning for the quarter is 120 crores. The investment provision is about 11 crores including SR 19 crores. Treasury related 11 crores, SR provisions 8 crores, total 19 crores. Standard assets 25.

Jai Mundhra: So second on gold loan sir. Is the environment is still not conducive for banks in general to grow that book or how do you see that book?

Shyam Srinivasan: We are growing gold loan, but most of it is agri gold loan. The retail gold loan growth has improved, but certainly nowhere near where we would like it to be. We are not against it, but the opportunity to grow gold loan not only for us, for most banks seem to be fairly modest.

Moderator: Thank you. We take the next question from the line of Hamsini Karthik from Smart Investor. Please go ahead.

Hamsini Karthik: Sir, I just want to understand your exposure to the second list of accounts referred for resolution under NCLT and also want to understand the trajectory of SME loans because we see that on the increasing mode over the last couple of quarters.

Shyam Srinivasan: Our SME growth is a very much sort of part of the strategy of the bank. In fact, that is our strongest area of the bank. When I say SME, I mean small, medium and micro and middle markets. So while we report SME as anything above 5 crores to 25 crores, we are seeing a growth of 20%. Our large part of our corporate is also in the mid-market which is in the 35-40. So that is the primary focus of the bank and that is growing quite well.

Hamsini Karthik: On the NPA side of SME loan sir?

Shyam Srinivasan: You would have noticed our NPAs have been traditionally around 100 to 120 crores on a growing denominator and that is how it will be and our SME book is the largely secured book. In fact when I mentioned strong recovery upgrades this quarter, lot of the recoveries have come from past period slippages on SME because they are well secured. Then the other question you had asked us about the second list of the NCLT, there are only two accounts and they are well provided for.

Hamsini Karthik: Well provided, I would assume above 50%?

Shyam Srinivasan: 60%., Above the regulatory threshold.

Hamsini Karthik: And if you could quantify the exposure?

Shyam Srinivasan: 55 crores.

Hamsini Karthik: And just one last point. I also noticed that the CASA ratio has slightly moderated compared to the de-mon levels. Any direction you would want to give us on that? Is the current trend more sustainable and the de-mon levels may not really happening?

Shyam Srinivasan: The de-mon period like many other banks, we saw lift up and that is moderated and you see sequentially Q1, Q2, Q3, every quarter it is improving. It is at 33% this quarter. We are certainly working to build it up to 35, but I want to qualify which I said in the last quarter call also all our CASA is at the card rate of 3.5% for savings. There are institutions which bid much higher to grow CASA at 6% which is like term. We have not done that. That is why our blended cost of deposits is trending down at 574 and that will continue. So I would look at the CASA not in standalone. I will look at CASA, retail granularity of the portfolio. You would have noticed 92% of Federal Bank's deposit is retail and combined that with the overall blended cost of deposits. As long as I get CASA at or around below that, it will be, 5.73 is our total cost of deposits and that has been coming down. Certainly, we are endeavoring to grow CASA very strongly, but to get back to 35% which is the de-mon number is our number one milestone.

Moderator: Thank you. We take the next question from the line of Arihant Bardia from Catalyst Global Equity. Please go ahead.

Arihant Bardia: My question with CASA, you just answered. I want to understand the cost-to-income trajectory as well for the next 3 years.

Shyam Srinivasan: We have guided in the beginning of this year and last year also between 50% and 51% and exit rate of about 50% for FY18 which we think we will hit. This quarter was slightly exaggerated because of two things. One is the denominator effect. The trading gains falling off by almost 65 crores compared to the previous period. Even half of it is there, the ratio would have been much different because the incremental cost increase is roughly about 20 crores for this quarter sequentially because I had said the three areas were investing into. One is the marketing and the brand, second is IT, and the third is in terms of the people related. There is a fourth that has arrived on the picture which is the impact of GST versus the service tax era. The GST era will add up about roughly 1.5%-2% increase in cost. It is not unique to federal. It is going to be a feature that is there. But that said, we are still guiding for a 50% exit rate if not Q4 FY18, it will be Q1 FY19.

Arihant Bardia: And with respect to your strategy, with respect to the relationship managers, are they are purely new workforce or shuffling of the existing workforce into newer roles?

Shyam Srinivasan: A large part of them are new recruits. There are some existing people who have been reallocated based on performance particularly on the retail side. On the corporate and SME, most of them have recruited and growing in the system.

Moderator: Thank you. We take the next question from the line of Dhaval Gada from Sundaram Mutual Fund. Please go ahead.

Dhaval Gada: Just couple of data keeping questions. What is the upgrade and recoveries during the quarter and write-offs and second is what percent of the book is now on MCLR?

Shyam Srinivasan: Recovery and upgrade this quarter is 220 crores, last quarter was 135. The previous year same quarter was 110. So recovery and upgrade as I mentioned has been very strong.

Dhaval Gada: And write-offs during the quarter?

Shyam Srinivasan: Nothing at all. And roughly 80% of the book is on MCLR.

Dhaval Gada: Okay. And any update on Fedfina and IDBI Federal?

Shyam Srinivasan: Fedfina is in very advanced stages. We are working through the term sheet and the reference documents. With appropriate approval, we can announce it in the course of the next two months or earlier. IDBI Federal, there is an entirely sort of detailed process underway and value discovery is going on. However, position on that will be informed by what we see as ultimate value that we will get. We are not biased to either sell or exit or upgrade, we are open for all options. But there is inherently very strong value which is getting discovered.

Dhaval Gada: Sure sir. And sir just lastly, what would be the differential in the incremental yield and back book yield on the corporate book?

Shyam Srinivasan: Again, it is very linked to the profile of the customer and the by segment, but roughly the…

Dhaval Gada: But on weighted average?

Ganesh Sankaran: The wholesale bank, yield will be about 9.5% presently on flow.

Dhaval Gada: Bank book, right, the overall current weighted average, right?

Ganesh Sankaran: Booking of the current flow is at 9.5.

Moderator: Thank you. The next question is from the line of Kunal Shah from Edelweiss Securities. Please go ahead.

Kunal Shah: So with respect to the wage revision which got effect from say November 2017, so do we see that impacting the overall salary base for us and have we started providing for it?

Shyam Srinivasan: Yes, we have. We have started providing two months of this quarter, we have provided I think 11 to 12 crores this quarter.

Kunal Shah: Okay. And despite that the overall employee cost is slightly on a lower side?

Shyam Srinivasan: They are slightly lower side because they were benefited by yield, the only upside if yield go up is some impact benefit comes on the pension cost.

Kunal Shah: Okay. And overall in terms of other OpEx, so whatever is the sequential growth which is coming in, that you highlighted would be also on account of GST?

Shyam Srinivasan: No, I didn't say entire thing. I said there are elements of that which is marketing, which is technology, which is this time there was a one-off cost of about 5 crores for re-carding for EMV which is a mandatory spend that we have to do and the other is GST. GST impact I said roughly about 2% increase versus a service tax era**.**

Kunal Shah: Okay. And is there any movement on the restructured asset side?

Shyam Srinivasan: This quarter, two of the accounts in addition to the existing standard restructured has become restructured, roughly say about 70 crores-80 crores.

Kunal Shah: No, but overall if that number is actually coming off…

Shyam Srinivasan: That is because some of the bonds have come down.

Kunal Shah: Okay. So largely it is on account of bonds?

Shyam Srinivasan: Yes.

Kunal Shah: Okay. And just one last question in terms of the overall AFS book and the duration of that?

Shyam Srinivasan: Usually duration we don't share but it is between 2-2.5.

Kunal Shah: And proposition of AFS?

Ashutosh Khajuria: We are quite close to the mandatory requirement of 19.5. We don't carry 6%-7% surplus SLR. That is why we are saved**.**

Moderator: Thank you. We will take the follow up from the line of Nagraj Chandrasekar from Laburnum Capital. Please go ahead.

Nagraj Chandrasekar: Yes. Just follow up on the question on CASA, so you said you are making progress towards a 35% which is a great idea. Any rough time horizon for this goal? Is this a 1-2 years goal, 2-3 years goal, 3-5 years goal, could you give us some indication of that?

Shyam Srinivasan: FY19. And here I want to point out is that, as close to the card rate as possible.

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

Nilanjan Karfa: Couple of questions actually. To begin with, how do you measure the performance of the RMs or rather for all of us sitting outside the bank, how should we look at that? Is there a way to figure this?

Shyam Srinivasan: At a very sort of aggregate level, you would look at the metrics that we are delivering in terms of growth and our overall performance and the relatively lower slippages and the credit quality. The RMs like I mentioned are spread across the range of businesses and therefore each of them carry KPIs which are very different from one and the other. And their rewards are heavily tacked to their volume growth and the flow through of the credit quality that they bring in and if it is a liability and a wealth management RM, they have different KPIs. So it is sharply targeted at each business vertical and the priorities of that vertical. The aggregate measure from an outside point of view would be one that we often discuss in terms of growth and the relatively high standard of the book quality.

Nilanjan Karfa: Right. Just a point there, because you mentioned you also assess the credit quality, I am sure that quality is assessed with a lag because loans typically won't default immediately.

Shyam Srinivasan: Yes, you are right and their rewards are also linked to that.

Nilanjan Karfa: Second is could you touch upon the NRI deposit flow, how is that working and while talking about it, could you split that out of your current account, savings account and term deposit, the percentage of NR deposits?

Shyam Srinivasan: Our total NR deposits of our entire franchise is close to 40%. Our NR deposits have grown very robustly and continue to grow. We are quite delighted in any market condition, we seem to be the port of first call**.** We are seeing that momentum continue. There are a lot of news reports on the overall NR volumes dipping in the country, but as you would have noticed our share of growth is only increasing further. So NR as a business, we are seeing strong growth and even through periods when there is reportedly job losses in the Middle East or slowdown, we have seen sharp growth because we are getting a larger share of the flow. Curiously or maybe more intuitively, whenever there is any sort of disruption or some kind of concern in the Middle East and those parts of the world, there is movement of money back into India and whenever there is movement of money back into India, we are the beneficiary. Also, the largest part of the segment of the market that we focus on is more "the must-send money to India" category and therefore when they must send, we are the preferred conduit for money to come in. So we remain confident that the NR growth will continue. The same cannot be said on the other side of the NR in terms of the credit performance which is where we have started being very careful on how we underwrite home loans and SME loans were linked to the NR and we have consciously slowed down some part of the business for almost a year.

Nilanjan Karfa: Right. But isn't it the case that at least on the NR liability piece, people who might be losing their jobs will obviously transfer the money back, isn't that why the volumes would be higher and therefore that need not be a proper metric of…

Shyam Srinivasan: You could say that if it is a one time and one off, but if you take across 8-10-12-14-16 quarters, you would see a pattern. We haven't seen any of that nature. Also I think the other important part which we often stress is that, as we sort of get our non-Kerala franchise growing quite well, we are seeing the NR in that part is now beginning to be a meaningful part, in the past it was 2%-3% of that, now 10% of that volume. So there is momentum there too.

Nilanjan Karfa: Right, okay. And can I have a couple of data points. You used to give out the current accounts spread between Kerala and outside Kerala, could we have that as well as for the comparable quarter last year and total employee count?

Shyam Srinivasan: Total employee count is now 11,950 thereabouts. The current account mix, sorry, you wanted to know the split, is it?

Nilanjan Karfa: Yes.

Shyam Srinivasan: 46% is network one, 54% is network two.

Nilanjan Karfa: Yes. I am sorry, and the final question. When you talked about the life insurance venture, what are the conditions under which you will sell versus retain the business?

Shyam Srinivasan: Maybe premature for me to answer because there is a process running and the good news is the process is bringing up even the first level of bidder have expressed good interest in value. So let that sort of mature which is about 30 days away and since this is three different partners and each one has a different priority, we have to be very sure that if one is exiting then the franchise value continues. So we want to make sure that if we are wanting to get the best value out of that, we want to remain invested till the right time comes. So I am not in a position to comment which way where? But debates are underway. We are thinking about 60 days, by mid-March we should have greater clarity on way forward. The good news is it is a substantial value which is emerging through the franchise.

Nilanjan Karfa: And correct me if I am wrong, the partners will have the first right of refusal, right?

Shyam Srinivasan: No. The original shareholder agreement visualizes that the two Indian partners if they want to dilute can offer it to the international partner who can go after the mandated limit of 49%.

Nilanjan Karfa: Not between the partners, Indian partners?

Shyam Srinivasan: No, unlikely that may happen.

Moderator: Thank you. We will take the next question from the line of Darpin Shah from HDFC Securities. Please go ahead.

Darpin Shah: Sir, can you provide sector wise breakup of the restructured book and what proportion of these exposures will be coming out of moratorium in next 1 to 2 quarters?

Shyam Srinivasan: Restructured book sector wise, the biggest is infra, which is power, road, aviation.

Darpin Shah: Sir, if you can provide the absolute or ballpark numbers for this exposure?

Shyam Srinivasan: Infra is about 800 crores. Aviation is about 250 crores and the balance is about 250 crores, iron and steel textiles.

Darpin Shah: And how much of these will be coming out of moratorium in next 1 to 2 quarters?

Shyam Srinivasan: Two accounts in this quarter.

Darpin Shah: Quantum?

Shyam Srinivasan: 300 crores.

Darpin Shah: And this will be largely from infra only?

Shyam Srinivasan: It is largely the aviation.

Darpin Shah: Okay. Fair enough. Sir how is the SMA-2 trending us and if you can just give some ballpark number on that?

Shyam Srinivasan: It is at all-time best.

Darpin Shah: Any ballpark number for it, sir?

Ganesh Sankaran: 33% reduction over the last 12 months.

Darpin Shah: Okay. Fair enough. And one last thing is sir, if you can provide absolute number of CA and SA?

Shyam Srinivasan: 4,800 is CA and 28,000 is SA, approximately.

Moderator: Thank you. The next question is from the line of Sreesankar from Prabhudas Lilladher. Please go ahead.

Sreesankar R.: A quick question on couple of factors. The growth that we have seen, is there any specific region that has seen an increased growth or is it uniform to most of the regions that we operate in?

Shyam Srinivasan: If you back out the corporate which certainly has a bias to Western India, everything else is equally paced between all our zones in the country and we continue to dominate our share of flow in Kerala, though we have slowed down on the SME side by choice. And across Mumbai, Chennai, Bangalore and North, we are seeing fairly equally distributed growth**,** actually it is also doing well.

Sreesankar R.: Okay. When you say that you have slowed down on MSME etc., SME, are we seeing some kind of headwinds or are you anticipating some headwinds out there?

Shyam Srinivasan: No, I think the data points to certain trend, I think it was an earlier conversation on the NR side and I said deposits are continuing to be robust, credit we are being watchful.

Sreesankar R.: The other side on education loans, where are we seeing the slippages, it is in Nursing or it is in Engineering or the high-ticket loans or on the lower quality. I shouldn't be saying lower quality but Nursing etc. Where are we seeing this stress maximum?

Shyam Srinivasan: As you know Sree, the large part of the education loans below 4 lakhs in the state of Kerala has largely been for Engineering and Nursing and therefore that pool of customers, when they are encouraged to wait for some dispensation are now tempted to not pay. Here I want to point out, in their mind, they have not defaulted because January 31 is a date when the government will take the decision on them. They should be standard on that date. We because it has crossed the 90-day mandatory, we have taken the hit. Every effort is by 31st January if they want the dispensation they may upgrade also, but that is for them to decide because to get the benefit of the state government they have to be standard on the date of benefit.

Sreesankar R.: Okay. Here you have mentioned in the presentation that your salary accounts have seen a 57% increase?

Shyam Srinivasan: Yes, it is.

Sreesankar R.: Where are we able to get these incremental salary accounts etc.?

Shyam Srinivasan: The 336 RMs that we talked off, in fact this quarter we did 125,000 payroll accounts and a large part of it is coming through either digital or what we call the instant account opening using tab banking and our digital capabilities are quite robust. We are seeing sharp growth. The RM model which often is been the question in terms of what is it doing for us other than getting credit is to also open doors in good corporate and mid-market where we can go and do the entire client and that is beginning give us a rich outcome. So the cross-sell focus is bearing fruit. And the RMs are heavily linked as in we have a corporate RM, we have a mid-market RM, retail RM and a customer service relationship manager. The combination works. That is for the personal loans.

Sreesankar R.: And this you have been able to get this incremental 125,000 at the cost of PSBs or other private sector banks?

Shyam Srinivasan: Would be a mix, I would think because the good corporates whom we are banking largely from the corporate side, some cards are multiple banks but we are seeing the sluggishness on some of the larger PSBs or willingness to take exposure, is helping the corporate to have a fresh look at banks like us, the new recruits. And we are getting the incremental flow of recruitments they are doing or the replacement hiring that they are doing.

Moderator: Thank you. The next question is from the line of M.B. Mahesh from Kotak Securities. Please go ahead.

M. B. Mahesh: Just a few questions. One, of late you started to increase your share of borrowings in your balance sheet which is kind of broadly highlights what is the differential that you are seeing on cost or what benefits are you getting here. Second, on the education loans, just a clarification, how much are you expecting in terms of repayment of the 70 crores of default. Third, if you could give us a breakup of your provisions and fourth GST momentum you have seen out there, are you actually seeing some amount of actual increase in revenues across all your clients that they are started reporting, or is this growth just a market share growth out there? Thanks.

Ashutosh Khajuria: So Mahesh first one is on the borrowing side. You would have noticed that our CD ratio has drastically improved. It is about 900 basis points YoY from about 76% to 85% now and as a result of that, we have taken some refinance from one of those institutions like NABARD, SIDBI and all which is CRR, SLR exempt. So that is coming on the borrowing side. It is not the call or the routine borrowing. It is a long term at a very competitive price. And that was taken in September, so I think we have the earlier refinances also getting matured. So it is partly replacement of the existing borrowing and traditionally something. So that is the component.

Shyam Srinivasan: You had four questions. One was on borrowings. Second I think was our expectation on what is the education loan recovery that we expect this quarter. Was that the question?

M. B. Mahesh: Yes.

Shyam Srinivasan: Early to tell, because every month the date gets reset by one. What was 31st October became December 31, December 31 became January 31. So if the January 31 deadline is a hard stop and there is no change, we would think at least 30% of them should be looking to become standard to benefit from the dispensation or the subsidy they are getting. But we will wait for that to mature and we will see how that plays out. What is the third question?

M. B. Mahesh: The breakup of your provisions for this quarter?

Shyam Srinivasan: I think we have mentioned 120 odd crores is credit provision, 20 odd crores is standard asset provision and 19 is investment provisions.

M. B. Mahesh: Okay. The last question was on a GST side, just trying to understand, have you started seeing some momentum in terms of credit demand on GST or is it simply market share gains that you are seeing out there?

Shyam Srinivasan: We are seeing market share gains very evidently across.

M. B. Mahesh: No. That question is in the reverse. We can see the market share gain. We are just trying to understand, on the ground have you started seeing people asking for increased credit for increased sales?

Shyam Srinivasan: It is nothing very pronounced. I would not say that there is any sharp change on that count.

Ashutosh Khajuria: Exporters had definitely looked at some additional finance because they were not getting the credit back. So that was there, from exporters there was certainly some demand. But that has also been taken care of now. That demand has receded.

Moderator: Thank you. We take the next question from the line of Rahul Gupta from Morgan Stanley. Please go ahead.

Sumeet: This is Sumeet here. So first question is on loan yields, so what percentage of the book is base rate linked and is it true that the bank hasn't reduced base rate since December 2015.

Shyam Srinivasan: We haven't changed base rate yes, you are right for the last two years. Loan book like we mentioned roughly 80% is on MCLR.

Sumeet: And why would that be like if I think about the base rate formula, deposit cost would have come down I presume, how is it that the bank has not cuts base rate?

Shyam Srinivasan: Base rate is not mandatory change. MCLR mandatorily changes. And as a comparative stance, so wherever possible we are trying to, anyway the spread above base rate is what customer is bothered. Base rate is not. So wherever there is an opportunity to give the customer the concession, we are working on it and it is heavily performance linked and credit quality linked.

Sumeet: Okay, second thing was on SME loans. The SME loans outside Kerala are doing quite well. Wanted to check if there is a difference with respect to collateral levels or LTV levels in the SME business that is...

Shyam Srinivasan: Non Kerala, the collateral is relatively lower. Kerala certainly is much higher.

Sumeet: And what would be the gap like?

Ganesh Sankaran: There is no gap, there is case to case. We are running a program on SME. We are doing individual bespoke credit underwriting.

Sumeet: Got it and the last question is basically, is it possible to indicative segment wise ROE that is federal bank could be making any corporate, retail and SME…

Shyam Srinivasan: To be honest, we want to be a little mindful that from April 18 we will give a better look on that because this has some moving parts, we are trying to get the best estimates of that. So I would buy time till at least end of financial year for us to make the better pitch on that.

Sumeet: Okay. And if I can squeeze in a last one, over the last 1.5 years the corporate banking has done very well in terms of loan mix and share of high quality loans continues to rise and to an extent, the pressure on loan yields would have been offset by improving loan to deposit ratio etc. How do you think about this incrementing, because high yielding corporate loans continue to rise, even in retail you are seeing an increase in share of mortgages and gold loan is not picking up that well. So from a margin perspective, if we continue to grow corporate and mortgage at a faster pace, does that mean margins could come under some bit of pressure and…

Shyam Srinivasan: Our business mix, if you take the last 3 quarters, sequentially each of our business is growing between 5% and 6% and that will continue and we have carved out between corporate, mid-market or the SME business of the commercial banking and then micro and that comes under business banking. Each of them are mandates, each of them are having a different yield mix. So there is business banking comes at roughly 11%. The corporate comes maybe at 9-9.5 like Ganesh pointed out and the mid-market around 10-10.5. So each of them have a different business mix and a business profile. And I think the margins like I have always mentioned has a function of many things, not just credit growth or mix of the credit book is one, second is the regular utilization of credit as opposed to period end higher CD ratio and this quarter it was also influenced by sharp recovery and upgrades. So we think the blend of all this should keep us in the 325-330 space.

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

Rohan Mandora: Sir, what are the incremental yields in SME within and outside Kerala, sir?

Shyam Srinivasan: I don't think there is any geographical difference of any nature and…

Ganesh Sankaran: It will be based on rating of the customer and the profile of the customer and less to do with geography of the customer.

Rohan Mandora: Okay, but sir what will be the average yields in SME and retail right now, incremental?

Shyam Srinivasan: SME is between 10.5 and 11.

Rohan Mandora: Because most of our customers was based out of Kerala, so the competitor is based out of Kerala, they are indicating much lower yields on the SME space. So just wanted to understand like what is driving the difference in terms of we being able to charge much higher yield in SME?

Shyam Srinivasan: I don't know which bank you are referring to, but they are indeed going into the market with much lower pricing. I do wish they did. But that apart, there is no one answer, it is just the ability to have a better engagement with client, full relationship and importantly we are able to offer much more than just credit.

Rohan Mandora: And sir like, what will be the outstanding SDR**,** S4A, 5/25 at the end of the quarter?

Shyam Srinivasan: Exposure to?

Rohan Mandora: SDR, S4A, 5/25 outstanding at the end of the quarter?

Shyam Srinivasan: I think that is not much of a relevance, but S4A, SDR, I think not a significant sum but tell you since you have asked the question.

Ganesh Sankaran: Last 2-3 quarters, we have not added anything on that count.

Shyam Srinivasan: SDR is less than 94 crores.

Rohan Mandora: Like I think during this concall, it was mentioned that we are slowing down in SME space in Kerala, SME lending in Kerala, so sir just wanted to understand is there any specific stress that we are seeing, just a strategy?

Shyam Srinivasan: I think when we say slowing down, it does not mean we are winding off. It is just that we are being watchful and given certain sectors of stress, given the impact of possible, the related NR stress and whatever, we have been watchful. And sectors like cashew and certain other Engineering Colleges, Medical Colleges, we are being very watchful.

Ganesh Sankaran: We are doing cherry picking, we are not slowing down.

Rohan Mandora: Actually like what will be the incremental retail yields overall and the portfolio elements?

Shyam Srinivasan: Retail is about 10.25 and the portfolio is a little higher.

Moderator: Thank you. We will take the next question from the line of Animesh Shah from L&T Mutual Fund. Please go ahead.

Animesh Shah: Sir, in the opening comments you mentioned that key monitorables in the coming quarter will be transition of restructured assets in the ARC receipts. Can you elaborate more on that?

Shyam Srinivasan: Yes, I can. I think the accounts that have been sold to ARCs, if they are anyway migrating from D1-D2-D3, the provisioning impact is the same as though they were on our book as per new regulations.

Ashutosh Khajuria: Despite having been sold to the ARC.

Shyam Srinivasan: So that is something that we are watching out for and we do anticipate some in this quarter.

Animesh Shah: Okay. And on restructuring any?

Shyam Srinivasan: Restructuring, we don't see any significant challenges this quarter.

Moderator: Thank you. We will take the next question from the line of Rahul Maheswari from IDBI Asset Management. Please go ahead.

Rahul Maheswari: I have one question that, what are your internal benchmarks in terms of your branch productivity and going from last 3 quarters we are finding the branch has been stayed at 1,252 kind of branches. So can you give more color that of what is the profitability or kind of the breakeven and branch expansion goal which for next two years kind of which will be taking place or you would be betting more on the employees salesforce which we added in the current quarter?

Shyam Srinivasan: I think I said in the last time and this time also, we haven't added actually not for 3 quarters, we have not added for 2.5 years. Our philosophy is branch light distribution heavy, which means we want to make sure that we are adding more feet on street and distribution power, all forms, digital, human beings, BCs and powering up our existing network. We may certainly look at certain branches may getting redistributed or relocated and rationalized, that we will do. The matrix for what we considered as branch profitability that I think range of them, so I can't sort of simply say one. And the traditional model people used to say x lakhs per branch, all that I think is passé, so I am not even venturing to give those numbers. But we have a range of parameters and we look at profitability, loss making, branches that are below base at any point in time and all those are being sort of continuously reworked. So effectively if you see our branch network, have grown the business, overall if we are growing 20 odd percent, the branches are also bringing in, pulling their weight for different businesses and there continue to be a large liability and fee generation which we will do. So the answer to your question is there are multiple metrics, but we are not looking to add many more branches, we are looking to add many more distribution opportunities.

Rahul Maheswari: So how many branches, any per annum you would be added or…?

Shyam Srinivasan: We have added for 2.5 years, so we may at best add another 50 in the next 18 months, but that is very subjective, we haven't looked at any large number consciously.

Rahul Maheswari: And due to this asset light strategy which you have adopted…

Shyam Srinivasan: Branch light.

Rahul Maheswari: Yes, branch light strategy, what kind of by FY20, the cost income we can come because the more of operating leverage would be coming if you are not adding and…

Shyam Srinivasan: I guided for 50% as the exit rate this year. We may keep around that guidance for 19 and 48 for FY20, 48 to 49.

Rahul Maheswari: On security receipts, SR, how much PCR has been provided?

Shyam Srinivasan: 870 is the NAV and 95 crores is the provision.

Moderator: Thank you. We will take the next question from the line of Anshu, an Individual Investor. Please go ahead.

Anshu: My question is related to the housing finance and seeing that the substantial portion of the growth for the bank is coming from housing finance, both from the retail as well as in the corporate side. So can you give a color on how it is really panning out in terms of the geography and more importantly in terms of looking at whether this is affordable housing which is growing or is it across the segment that the growth is being seen?

Shyam Srinivasan: It is very widely spread and affordable housing also have multiple descriptions. Our average ticket size on the housing loan is about 35 lakhs. So it will be partly in affordable and partly in the regular housing loans. So there is no bias to that. Bulk of our growth is coming in markets like Mumbai and Delhi and Pune where the average ticket size is higher.

Anshu: And the second question that I have with respect to this is that, what is the incremental, the loan segment which has grown in the last quarter, what is the rate at which we have been lending to the housing finance companies?

Shyam Srinivasan: Housing arena is very competitive. Whatever is the best banks are offerings… Housing finance or housing?

Ganesh Sankaran: It is like any other corporate loans for us.

Anshu: Yes, in the corporate segment, yes.

Ganesh Sankaran: It is like any other corporate loans. We don't have a specific rate for housing finance company.

Anshu: So what would be the rate at which you are lending to them?

Ganesh Sankaran: As we said, closer to 9. The corporate book flow is at 9.

Moderator: Thank you. We will take the next question from the line of Jayant Kharote from JM Financial**.** Please go ahead.

Jayant Kharote: I just wanted to know the number for our portfolio buyout this quarter?

Shyam Srinivasan: Nothing. Zero. We haven't done any portfolio buyout for almost a year now.

Moderator: Thank you. We will take the next question from the line of Pritesh Bumb from Prabhudas Lilladher. Please go ahead.

Pritesh Bumb: Sir, your tier 1 quarter-on-quarter hasn't changed, anything to read on that?

Shyam Srinivasan: The credit risk book has improved. So there is no major change in Q2 to Q3, the risk weightage has not changed, so tier 1 has not changed much. So there is not much risk weight change. In fact, the portfolio has improved in quality. So the risk weight has improved.

Pritesh Bumb: So the absolute number also will get impacted from that, is it?

Shyam Srinivasan: I would think so, yes. Could you please repeat the question?

Pritesh Bumb: Sir what I was asking is the tier 1 absolute quarter-on-quarter has not changed much.

Shyam Srinivasan: It has moved from 14.63 to 14.41, in the CRAR and almost all of it is tier 1.

Pritesh Bumb: Sir, second question is on the fee income side. So we have seen good growth in the advances book, but the gross income has not moved much quarter-on-quarter basis?

Shyam Srinivasan: I think fee income ex trading gains is tracking credit growth and we are keen to push that up further which we are working on. So if you take Y-on-Y, sequentially the number is a little jinxed because of some of the one-offs which is a reversal. But the credit growth and the fee income is tracking in fact, processing fees and effects have grown more than 20% each of them. The only thing on the other income which is trending below, largely driven by where yields are. This quarter we saw a sharp fall, but other income we are not saying at the top notch, we are growing 20%.

Pritesh Bumb: So the core fee income will continue to grow at a good pace?

Shyam Srinivasan: Yes. We are keen to do it at least 200 basis points higher than credit growth but that is still work to do. In fact, we have internally said and from next year we will look at our share of fee, of course there is no substantive market information but we will try and capture that sort to see like way growing our credit growth what is our fee market share growth also.

Moderator: Thank you. We will take the next question from the line of Sanket Chheda from IDFC Securities. Please go ahead.

Sanket Chheda: Yes sir, you said that slippages will be similar next quarter for couple of quarters. So it would be around 400 crores is what you said or it is barring that education loan?

Shyam Srinivasan: If you add the impact of any potential slippages on account of the RBS that has come through, we think roughly between 350-400 crores it should be for Q4. So whatever education loan will get replaced by any other bulk that we will see.

Moderator: Thank you. We will take the next question from the line of Gaurav Gyani from Centrum Broking. Please go ahead.

Gaurav Gyani: Just some clarity on this education loan. I probably joined the call a bit late. So can we see such more instances in other states also and if I could have the quantum of exposure towards education loan segment and the Kerala part? Thanks.

Shyam Srinivasan: Largely, our education loan book is in Kerala. I think roughly about 500 odd crores is in Kerala. This is hopefully a one-time event in one geography. If it spreads, it is good, but our book ex Kerala is very small and in Kerala for the last 6 months, they have been deferring the date for keeping the account standard and the promise of some kind of discount of I think 40% waiver has been offered by the state government. But that date keeps shifting. It was October 31, then became December 31 and then become January 31. And because by the time the account had slipped, even bona fide customers who are paying are now looking forward to this benefit and therefore we have taken the hit. Do we anticipate this in across other states, not quite and if it does, it doesn't affect Federal Bank.

Gaurav Gyani: Sure. Just one more thing sir. So when the government says that the 40% will be waived which means they would probably make good the 40%...

Shyam Srinivasan: Yes. That is the stated position, for which the government insists that the client should be standard to avail of the benefit.

Management: As on the cutoff date.

Gaurav Gyani: Got that. Sir just one last question from my side. Congratulations that this quarter we haven't had any write-offs. So the new book has actually come in our advances, is it a fair assumption?

Shyam Srinivasan: Yes, but the write-offs that we ever did were all 100% provided. Vintage of the account dependent on sort of the different vintages. But that there was no write-offs this quarter, is certainly right.

Gaurav Gyani: Yes. So can this be a trend going forward, was my question?

Ashutosh Khajuria: In case the migration happens from D2 to D3 and then the provision requirement is 100%, there is no advantage in keeping it at 100, because that simply inflates the balance sheet. You have the 100% provision on liability side and you have the asset on the other side which according to RBI's requirement is directive, needs to be provided fully. So in that case write-off is the better option.

Gaurav Gyani: Sure sir. Can we expect some movement from D2 to D3 going forward?

Shyam Srinivasan: That is a normal run and I mentioned in particular, some of the SR accounts we do anticipate this quarter.

Moderator: Thank you. We will take the next question from the line of Sreesankar R from Prabhudas Lilladher. Please go ahead.

Sreesankar R.: Last quarter we had 1,343 crores of standard restructured and this quarter is 1,425, where have you seen the incremental restructuring?

Shyam Srinivasan: As we mentioned, two accounts have moved.

Sreesankar R.: In slide #7, out of the total restructured NPAs, total is 1,611 versus 1,746, in Q2.

Shyam Srinivasan: Correct.

Sreesankar R.: NPA is 186 versus 403 last quarter.

Shyam Srinivasan: Correct.

Sreesankar R.: So the difference of that NPA is 220 crores loan loss provisions that you provided, right?

Shyam Srinivasan: No, this is a sale of bonds also. We have had bonds which we have sold.

Moderator: Thank you. We will take the next question from the line of Sneha Ganatra from Subhkam Ventures. Please go ahead.

Sneha Ganatra: Sir, what is the exposure in NCLT and how much provision you are holding?

Shyam Srinivasan: I think we mentioned, maybe you came in late. I think the two accounts are well provided. We have more than 60% provision.

Sneha Ganatra: And considering the Ind-AS and the other provisions, what would be your credit cost guidance for next year?

Shyam Srinivasan: We don't know when Ind-AS is going live. But the credit cost guidance, if you take we have had some volatility over the last 3-4 quarters. This quarter was very good at 59, the previous quarter was 71 and there was another quarter at around 75. We think between 60 and 65 basis points next year, all things being the same.

Moderator: Thank you. We will take the next question from the line of Shripal Doshi from Equirus Securities. Please go ahead.

Shripal Doshi: Sir, this is basically regarding your yields on advances. So in the presentation, the yields and advances mentioned at 9.54%, but in the earlier conversation you have mentioned that for the corporate, it was around 9 and for retail 10.2 and for SME 10.5. So basically not able to understand the mix over here?

Shyam Srinivasan: There are two parts to the question. One is when we say that is a blended, right, there are some tickets maybe, you are asking for what are the average run rate on the new? That is the number we gave. But the blend of the portfolio could have somebody who would have been lent at MCLR, a large business. So it is a mix and therefore the 9.54 is the blended yield on the total asset book.

Moderator: Thank you. We will take the next question from the line of Dhaval Gada from Sundaram Mutual Fund. Please go ahead.

Dhaval Gada: Just a follow up from the previous question. So could you just give the blended yield for the retail, corporate, SME and agri again, just so that we can reconcile the 9.54, thanks.

Shyam Srinivasan: Agri is around 10. Retail is about 10.4, business banking is about 11.4, commercial banking is about 10.2, corporate is almost 9.

Moderator: Thank you. The next question is from the line of Sanket Chheda from IDFC Securities. Please go ahead.

Sanket Chheda: Yes sir, in this quarter there was a sharp jump in investment, for quarter-on-quarter 13%. So what could have led to this sharp jump?

Shyam Srinivasan: Sorry which slide are you referring to? I am sure you are looking at our investor deck? Sanket?

Sanket Chheda: Yes, investments.

Shyam Srinivasan: No which part, have you looked at our investor deck or where did you pick that up from?

Sanket Chheda: Investor deck only. This quarter the quarter ending investments are 29,775, right?

Shyam Srinivasan: YoY has increased 13%, not QoQ.

Management: YoY is 5.03%, YoY also.

Sanket Chheda: No, sir it is QoQ, if you see in Q2, the investments were 26,317 crores and this quarter 29,775. So there is a sequential jump of 13%.

Ashutosh Khajuria: As the deposits have grown, accordingly some SLR purchase has been made and SLR purchase has been made in HTM mode because the deposits have gone up. Yes, there is no other increase.

Sanket Chheda: Sorry sir, what was that?

Ashutosh Khajuria: Basically from 31st December if you see, 31st December last year same time, the investments have had actually fallen by 1,500 crores. So that you have to replenish plan for your deposit growth and accordingly, the statutory SLR requirement is there in anticipation of deposit growth as well as the actual deposit growth that has happened. So it increases only in SLR segment and that too for HTM category. The YoY growth if you see, it is 5% only. YoY, December over December is 5%, from 28,500 crores to 29,000 odd.

Sanket Chheda: Yes. And sir would you provide any guide on your off balance sheet products? Is there any increase or how you want to picturize that going forward, your non-fund exposure is very low, I guess. So off balance sheet items like bank guarantees and letter of credits and all…

Shyam Srinivasan: Often we have explained on our call, we don't look at it, ultimately it is the credit exposure on the clients. So whatever gets us the best return we will and prospectively doing off balance sheet need not necessarily be a big benefit given the fact that you are going to look at return on risk weighted assets. So effectively…

Ashutosh Khajuria: Plus, ECL is to be calculated as per IFRS…

Shyam Srinivasan: So it is not a very period when you are trying to show high ROA by keeping some part of the earnings outside the balance sheet has made sense, but we are not looking at anything. But short answer is, if it is valuable we will do it.

Moderator: Thank you. We will take the next question from the line of Arjun Tandon from Matsya Capital. Please go ahead.

Arjun Tandon: Just wanted your comments on the RBI divergence. You mentioned you have not received the report, but they have completed the divergence. But you also said the bulk will be replaced, the education loan bulk would be replaced?

Shyam Srinivasan: Sorry, I didn't say RBI has completed divergence. We are not saying that there is no divergence. We are a bank that last year had almost nothing. So we are certainly in dialogue. We don't anticipate a large number. Whatever it is, it will be accommodated in the numbers I guided for.

Moderator: Thank you. The next question is from the line of Harish Kapoor from IIFL. Please go ahead.

Harish Kapoor: Most of the questions have been answered, just on the asset quality front, just wanted to get some sense. So you said that next quarter the number on the additions could be around 400 to 450 which is including the RBI's recognition. But on the education loan front, I wanted to understand, so you have 300 crores exposure and the subsidy that the government is giving, is it only on below 4 lakhs and if that is so, then what is the quantum of exposure from 300 crores for that?

Shyam Srinivasan: The 4 lakhs and below is where this education loan waiver is. The large part of the numbers that I mentioned is in that. But whatever needs to be addressed has been addressed this quarter. So we don't expect that number to change.

Harish Kapoor: So all 300 crores is basically the number you are saying, that is below 4 lakhs.

Shyam Srinivasan: Yes.

Harish Kapoor: And 70 crores has been provided as additions now. So what is the provision for these specific bulk assets that has been provided? What is the provision on this that you have?

Shyam Srinivasan: Normal version. Whatever IRAC norms are.

Harish Kapoor: 15%?

Shyam Srinivasan: But our overall coverage is 70%.

Harish Kapoor: Yes, okay. But then this could also kind of increase substantially, right, in Q4?

Shyam Srinivasan: Means what?

Harish Kapoor: As in if you could see more higher stress that could come through in Q4?

Shyam Srinivasan: I know, the last date for that is January end. So unlikely that would change, if anything, it should improve.

Ashutosh Khajuria: If it improves between today and 31st January.

Moderator: Thank you. The next question is from the line of Roshan Chutkey from ICICI Prudential Asset Management. Please go ahead.

Roshan Chutkey: So, how many of the 330 RMs that we have are assigned to SME business and how many to the corporate business?

Shyam Srinivasan: 60 for SME and 55 for corporate.

Roshan Chutkey: And this brand distribution mix in rural geography particularly is pretty low, in lower teens, any…?

Shyam Srinivasan: Our rural plus semi urban is almost 65% of our network.

Roshan Chutkey: So don't you face any regulatory backlash because of this?

Shyam Srinivasan: No, none at all. We are very much within all our guidelines.

Moderator: Thank you. There are no more questions. So you can give your closing comments sir.

Rajanarayanan N: Thank you all for patiently joining the call. Thank you. This call comes to a close. Thanks.

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