"HDFC Bank Limited

Q3 FY'23 Earnings Conference Call"

January 14, 2023

MANAGEMENT: MR. SRINIVASAN VAIDYANATHAN – CHIEF FINANCIAL OFFICER – HDFC BANK LIMITED

Moderator: Ladies and gentlemen, good evening, and welcome to HDFC Bank Limited Q3 FY '23 Earnings Conference Call on the Financial Results, presented by the management of HDFC Bank. 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 brief commentary by the management. Should you need assistance during the 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. Srinivasan Vaidyanathan, Chief Financial Officer, HDFC Bank. Thank you, and over to you, sir.

Srinivasan Vaidyanathan: Okay. Thank you, Tanvi. Good evening. Welcome to all the participants. Greetings of the New Year. Now let's start with some context on the environment that we operated in the quarter that gives a background of how we operated.

High frequency indicators suggest that domestic economic activity held up in Q3. GST collections continued to be robust, remained above INR 1.4 lakh crores since May '22. In December, GST collections stood at INR 1.5 lakh crores compared to INR 1.3 lakh crores in the prior year December. Manufacturing PMI has remained in the expansionary zone and is at 57.8 as of December and also the services PMI is at a six-month high of 58.5 in December.

Healthy trend in government capital spending also bodes well for industrial activity, spent almost 60% of budget estimates during April to November versus 49% in the prior year. On the consumption side, we had our cards issuing spend growing at the rate of 27% year-on-year, reflecting good consumer demand. Rabi crop sowing looks encouraging, up 4.5% above last year's level.

As you know, the RBI raised the policy rate by 35 basis points to 6.25% and kept the policy stance unchanged at withdrawal of accommodation. There are risks stemming from the possibility of global slowdown. Reopening in China amidst rising COVID cases in many parts of the world and continued geopolitical tension. However, strong consumer demand boosted by fiscal spends and higher Agri produced from rabi crop are likely to keep the Indian economy stimulated. We estimate the GDP growth to be around 7% for the financial year '23. Let's go through certain things at a high level.

On the distribution, we added 684 branches during the quarter, taking the total to 841 branches in the year so far. Gold loan processing are now offered in 3,938 branches, an increase of 978 branches in the current quarter and up 3x over March '22. Payment acceptance points growth has picked up pace as a smarter platform with momentum taking the total to 3.99 million year-on-year growth of 45%.

Wealth management is now offered in 691 locations. Through hub-and-spoke model, we have expanded by 189 locations in the quarter. On the CRB side, our SME businesses are present in more than 90% of the districts. Rural business reach expanded to 1.51 lakh villages and is on track to reach the objective of 2 lakh villages.

In the customer franchise building process, during the quarter we added 5,863 people and 32,478 people over the year. Our people have acquired 2.6 million new liability customer relationships, exhibiting a healthy growth of 12% over prior year. On cards, we issued 1.2 million cards during the quarter, total card base is now 17 million.

We progress in our pursuit to focus on granular deposits. The deposits total amounted to INR 17,33,000 crores, an increase of 3.6% over prior quarter and up 19.9% over prior year. In retail deposits, we added INR 67,000 crores during the quarter and INR 258,000 crores since prior year. Retail now constitutes about 84% of our total deposits and have been the anchor of our deposit growth.

CASA deposits recorded a strong growth of 12% year-on-year, ending the quarter at INR 762,000 crores, with the CASA ratio of 44%. Retail CASA grew by 14% and retail total deposits grew by 22% year-on-year. Retail current account which constitutes 70% of our current account deposits grew by 14% year-on-year, while our wholesale current account de-grew by 4% year-on-year.

Time deposits registered a robust growth of 27% over the prior year, ending the quarter at INR 970,000 crores. On the advances, it ended the quarter at INR 15,06,000 crores, grew by 1.8% sequentially and 19.5% over prior year. This is net addition of approximately INR 27,000 crores during the quarter and INR 246,000 crores since prior year. Gross of sell downs, IBPC, we grew advances by 23.6% year-on-year and 3.3% quarter-on-quarter.

Our retail advances growth was robust, domestic retail grew by 21.4% year-on-year and 4.7% quarter-on-quarter. CRB, which drives our MSME and PSL book for most part, continued its momentum with an year-on-year growth of 30% and quarter-on-quarter growth of over 5%.

Wholesale segment witnessed a strong year-on-year growth of 20%. Corporate Bank initiatives across new-to-bank PLI, MNC and supply chain finance, continue to be a focus, allowing to diversify revenue pools from new customers, products and sectors. We expect demand from loans from NBFC telecom PSUs, retail and infrastructure sectors to sustain.

On the digital front, the bank continued its momentum on the technology and digital transformation agenda to provide greater customer experience, through our digital and enterprise factory. Progress on the key digital initiatives in the quarter, SmartHub Vyapar our one-stop merchant solutions app has further enhanced with the addition of new features in the current quarter such as instant QR, a revamp of ETB journeys and enabling onboarding of new-to-bank customers digitally. As of December end, over 1.9 million small businesses are on smarter platform, the platform is adding more than 80,000 merchants per month.

HDFC Bank One, the customer experience hub, the solution which transformed our on-premises contact center into a singular centralized service platform has now been further expanded across more locations in India now at seven locations. It enhances our customer relationship management process using AML and conversations BOT enabling round-the-clock self-service. With the rollout of HDFC Bank One, we have witnessed significant improvements in our customer engagements such as 39% reduction in case resolution time and a 64% reduction in turnaround time and an average reduction of 324 seconds in handling time in our care centers.

Express car loans is a first of its kind end-to-end digital service, enabling instant and hassle-free car disbursals. This channel contributes now 17% of our new car loan volumes. PayZapp, in the previous quarter, we launched PayZapp 2.0 to a closed user group, as we mentioned before. In this quarter, this was made available across the bank personnel, as well as app stores for early adopters. We have received encouraging response from the users of PayZapp 2.0. The existing 31 million registered users on the erstwhile PayZapp will be progressively transitioned to the new app. In Q3, we received a total of 315 million visits on our website, over 100 million unique visitors over the quarter at a year-on-year growth of around 30%, reflecting enhanced engagement in our digital properties.

Our continued investments in expanding our distribution network by adding people and branches combined with our focused digital offering and relationship management to fuel growth. Balance sheet remains resilient, LCR for the quarter was at 113%, capital adequacy ratio is at 19.4% with a CET1 at 16.4%, including profits for the nine months ended 31st December '22.

On the revenues, which ended the quarter at INR 31,488 crores, on a reported basis grew 18.3% year-on-year. Core net revenues were at INR 31,236 crores excluding net trading and mark-to-market income grew by 22% over prior year and 8.2% over prior quarter, driven by an advances growth of 19.5% and deposits growth of 19.9%.

Net interest income for the quarter at INR 22,988 crores, which is at 73% of net revenues, grew by 24.6% over prior year. The core net interest margin for the quarter was at 4.1% and this excludes one-off interest income on income tax refund of about 5, 6 basis points. Prior year and prior quarter were also at 4.1%. On interest earning asset basis which appears to be industry norm, the core net interest margin was at 4.3%, again at the similar levels to prior quarter.

Moving on to details of other income. Fees and commission income constitutes about 3/4 of the other income was at INR 6,053 crores and grew by 19% over prior year and 4% over prior quarter. Retail constitutes approximately 93% of fees. FX and derivatives income at INR 1,074 crores was higher by 13% compared to prior year of INR 949 crores. Net trading on mark-to-market income were positive INR 261 crores. The mark-to-market gains are mainly from AFS investments.

Prior quarter was a negative INR 253 crores and prior year was a gain of INR 1,046 crores, which were then opportunistic from our investments portfolio. Other miscellaneous income of INR 1,112 crores includes recoveries from written-off accounts and dividends from subsidiaries. Excluding net trading and mark-to-market income, total other income at INR 8,238 crores, grew by 15% over prior year.

Operating expenses for the quarter were at INR 12,464 crores, an increase of 26.5% over prior year. We added 1,404 branches and 1,769 ATMs since last year. As I said, we added 684 branches during the quarter, 841 branches during the year, taking the total network strength to 7,183 branches. Cost to income for the quarter was at 39.6%.

Moving on to PPOP, our core PPOP grew by 19% year-on-year. Our Pre-Provision Operating Profit was at INR 19,024. Pre-Provision Operating Profit for the quarter is 6.78 times the total provisions. Coming to the asset quality, the GNPA ratio was at 1.23% compared to 1.26% in prior year and 1.23% in prior quarter. Out of the 1.23% about 17 basis points are standard, thus the core GNPA is at 1.06%. However, these are included by us in NPA as one of the other facilities of the borrowers in NPA. GNPA ratio, excluding NPAs in agricultural segment was about 100 basis points. Prior year was at 104 basis points and prior quarter was at 103 basis points.

Net NPA ratio was at 33 basis points, prior year was at 37 basis points and preceding quarter was also at 33 basis points. The slippage ratio for the current quarter is at 42 basis points or about INR 6,600 crores. The slippage ratio for the current quarter excluding Agri, which is a seasonal. December quarter impact was at 35 basis points or about INR 5,300 crores. During the quarter, recoveries and upgrades were INR 3,100 crores, approximately 21 basis points. Write-offs in the quarter were INR 3,100 crores or approximately 21 basis points. Sale of NPA of about INR 200 crores in the quarter.

Moving to the restructuring. The restructuring under the RBI resolution framework for COVID-19 as of December end stands at 42 basis points, about INR 6,400 crores. In addition, certain facilities of the same borrower, which are not restructured is approximately 8 basis points of INR 1,100 crores plus totals to 50 basis points. The COVID restructuring in the prior quarter was at 62 basis points. Now moving to the provisions, the total provisions reported were INR 2,800 crores as against INR 3,000 crores in the prior year and INR 3,200 crores in the prior quarter.

The provision coverage ratio is at 73%. At the end of current quarter, contingent provisions and floating provisions were close to prior quarter level at INR 10,800 crores after utilization of approximately INR 200 crores. General provisions were INR 6,600 crores, contingent provisions were INR 3,400 crores and floating provisions were INR 1,451 crores. Total provisions comprising specific floating contingent and general were about 166% of gross non-performing loan. This is in addition to the security held as collateral in several of the cases. Floating contingent and general provisions were about 1.15% of gross advances as of December end.

Coming to the credit cost ratios. The total annualized credit cost for the quarter was at 74 basis points, prior year was at 94 basis points and prior quarter was at 87 basis points. Recoveries which are recorded as miscellaneous income amounted to 21 basis points of gross advances for the quarter as against 25 basis points for prior year and 22 basis points for prior quarter.

The total credit cost ratio, net of recoveries was at 52 basis points in the current quarter as compared to 69 basis points in prior year and 64 basis points in prior quarter. The profit before tax was at INR 612 crores The net profit after tax for the quarter was at INR 12,260 crores, grew by 18.5% over prior year. Now some highlights on HDB Financial Services, this is on an Ind-

AS basis. The momentum in disbursements continued across all three business segments during the quarter, registering a healthy growth of 41% year-on-year, 18% sequentially.

Customer franchise grew to 11.2 million customers, adding 2.6 million over last year. HDBFS has started to augment the distribution network and opened 14 branches in the current quarter, aggregating to 1,421 branches spread across 1,020 cities and towns. The loan book as on December end stood at INR 65,100 crores with a secured loan comprising 73% of total loan book.

Net revenue for the quarter was INR 2,233 crores, growth of 12.7% over prior year. Provisions and contingencies for the quarter were INR 313 crores compared to INR 540 crores for prior year and INR 351 crores for prior quarter. Credit cost for the quarter were at 195 basis points as against 358 basis points for prior year and 225 basis points for prior quarter. Quality of the book continues to see sustained improvement.

Stage 3 as at December end, saw a significant improvement and stood at 3.73% as against 4.88% in the prior quarter, reflecting sustained healthy collections. Provision coverage on Stage 3 book stood at 57%. The PCR on the secured and unsecured book stood at 54% and 85%. Profit after tax for the quarter was INR 501 crores against INR 304 crores for the prior year and INR 471 crores for the prior quarter. HDBFS ROA stood at 3.12% and ROE stood at 18.8%.

Earnings per share in HDB for the quarter was at INR 6.34 and book value per share as of quarter-end was INR 137.52. HDBFS remains well capitalized with total capital adequacy ratio at 20.5% and continues to step-up disbursements leveraging strong distribution spread across 1,400 plus branches. Now coming to HDFC Securities. HDFC Securities Limited added nearly 0.9 million new clients in 12 months to December, taking the client base to 4.3 million.

HSL has a network of 210 branches spread across 147 cities. Digital offerings continue to enjoy good traction in the market, which around 93% of active clients utilize the services using the digital platforms of the company. The total reported revenue for the quarter was INR 505 crores for HSL against INR 536 crores in the prior year. And net profit after tax was INR 203 crores as against INR 258 crores in prior year. Earnings per share in the quarter was INR 128.1 in HSL and book value per share is at INR 1,114.

Now in summary, tailwinds from the economic momentum, fiscal and monetary policies have provided conducive environment for growth, by delivery of our full suite of products and services. Our results reflect robustness across various parameters, continued momentum in deposits growth at about 19.9% and retail deposits growth of 21.6%, advances growth of 19.5%.

Core operating profit growth, net of trading and mark-to-market income was 19%. Profit after tax increased 18.5%, delivering the return on asset of about 2.2% and return on equity of over 18%. Bank's earnings per share reported in the quarter is at INR 22. The book value per share stands at INR 479.80. With that, may I request the operator to open up the line for questions. Thank you.

Moderator: The first question is from the line of Kunal Shah from ICICI Securities.

Kunal Shah: So firstly, with respect to…

Srinivasan Vaidyanathan: Kunal, just one second. The team told me that I have to correct two things. I think, I was referring to the profit before tax is INR 16,218 crores, I think was referring somewhere. And the contingent provisions, I said INR 3,400 crores or something it is INR 9,400 crores, that's all I just want to -- because I was referring wrong places. Now go ahead, Kunal.

Kunal Shah: Sure. Yes. So firstly, on opex and particularly the employee cost side, no doubt we have added quite a lot of employees over last couple of quarters. But was there any other extraordinary within that wherein maybe the sequential growth was also quite high and both as well as year-on-year, so if you can highlight on that part? Yes.

Srinivasan Vaidyanathan: One is that normally the third quarter is the seasonal with a lot of activity in that time period. That's number 1. Number 2, on the people cost, apart from adding of people both for business growth and branches, there is also another tranche of ESOP and RSU that would come in, that's about I think INR 250 crores or INR 300 crores approximately, that would come in, that's part of that, it's a business as usual. I wouldn't call it a one-timer, that's part of the business which is embedded there, which would be compared to prior year. And even prior quarter because the ESOPs were effective October and the RSUs were also effective about end October or something. So those part of the cost which is there.

Kunal Shah: So INR 250 crores to INR 300 crores odd?

Srinivasan Vaidyanathan: Correct. Yes.

Kunal Shah: Sure. And secondly in terms of the other interest income, particularly around about say INR 800 crores odd. So, what does that actually pertain to? Because I think that's what is driving the NII, otherwise broadly when we look at it in terms of the advances investments and the expenses, then NII growth seems to be round about 22-odd percent? Yes.

Srinivasan Vaidyanathan: See the other interest income if you look at the class 41 or something that has got certain income that comes from non-lending. It could be income on RIDF deposits kind of thing will be there. That's one. On the other one, I think, I called out, which is about 6 basis points is the interest on tax refunds.

Kunal Shah: Interest on?

Srinivasan Vaidyanathan: Tax refunds, IT, income tax refunds.

Kunal Shah: Yes. Tax refunds. Okay. So that quantum would be around about 300 pointed out, so 6 odd basis points is what they highlighted. Okay, got that.

Srinivasan Vaidyanathan: Above 300. Yes.

Moderator: The next question is from the line of Suresh Ganapathy from Macquarie Capital Securities. Please go ahead.

Suresh Ganapathy: Yes. Srini, so two questions. One is on deposit accretion itself. So, if you look at Q2, the deposit accretion is INR 600 billion or if you look at purely in retail deposits, it's INR 670 billion and the previous quarter was INR 680 billion on overall deposit. The initial guidance was that eventually you want to take it to INR 1 trillion with every quarter showing an improvement, but that has not happened in 3Q.

In fact, 3Q has shown a decline over 2Q in terms of absolute accretion of deposits. So, what's happening here, are we on track to get that INR 1 trillion accretion? Any color on that would be great, Srini.

Srinivasan Vaidyanathan: Good point, Suresh. Yes, indeed, our objective was to take that 60,000 to 68,000 to 80,000 to 100,000 as we go. And yes, this quarter, if you look at retail came in with INR 67,000 crores. The retail came in quite well. Yes, it didn't come in as much as what we thought. We had expected that it to be 80,000 or above, north of 80,000 or above, but it came in at 67,000. Within this kind of right away, we did put in audacious goal and in terms of how we want to get there and achieve. And it came in at 67,000.

But we are still the mindset on the drive and the distribution network and leveraging of our existing relationships are in full core. And we believe that in this quarter, more consumer spending has happened broadly in the country, and we see that in our own customer base too. If you look at our cards, as an example, card spend, the retail card spend growth is 27%. So, people are spending in other things that they want to do. So that's part of what has happened. But we are still getting on track to be growing that sequentially up.

Suresh Ganapathy: And the next two questions, is first on margins. Your margins are flat Q-o-Q or Y-o-Y also for that matter, whether you look at repo on assets or interest earning assets. My point here is Srini, bulk of the deposit rate hikes have actually happened between September to December. You can see actually all banks. even Post, the SBI and even yourselves included have hiked deposit rates quite aggressively.

So, if you have not seen a margin expansion this quarter, especially when deposit rate hikes are yet to flow through, what happened next quarter when some of the deposit repricing? Or at least the incremental flow will be at a higher rate. Do you think you can sustain the current level of margins or there could be any margin pressure?

Srinivasan Vaidyanathan: Again, very nice and very correctly you're asking that. It is correct that to expect that deposit pricing factoring in as we go along would start to increase because if the prices have started and it will have a full quarter impact, and if there is one more rate hike and there will be further coming in on the deposit costs. But along with that, the loan pricing also happens.

Our position is more or less is kind of a balanced. When the deposit pricing goes up, we also get up on the pricing on the assets. So, if you look at some of our -- MCLR is a good indication to see while that not all loans are there, but it's not an enormous amount of retail loans go off MCLR. And then there are certain other SME type loans that also based-off the MCLR.

So, if you look at that, we have enhanced that more than the deposit funding do. So that means we are catching up on the asset yield also along with that, so that's the second thing to keep in mind.

The third thing, the margin pickup, I think over a period of last four, five quarters we have been saying that the margin is a function of the mix of products. To the extent deposit goes up, the asset yield goes up to keep the margin constant or thereabouts within a small range. But the margin going into the middle to the higher end of the 4, 4.5 is a function of the mix of wholesale and retail.

Still despite retail growing 5%, up sequentially, the mix is still 45 retail, 55 wholesale, the Basel classification is still at 45, 55, right. And couple of few years ago before COVID, few years ago it was 53% to 55% retail. So that list needs to change for the margin to move up. But the other question that you asked is the margin under pressure? Yes, we are cognizant that we need to keep up on the yield to keep pace with the deposit cost that goes up.

Suresh Ganapathy: And lastly, anything you've heard from RBI with respect to any of the statutory relaxations or any other relaxations that you have thought? If not then, what do you think could be the timeline to hear something on that front?

Srinivasan Vaidyanathan: Not yet, Suresh, not heard yet. But we would expect it within the next month or two there is no particular timeframe, this is not particular schedule. For context, is that the merge process is progressing, the NCLT final hearing is on 27 January. And so there upon once it's adjudicated, and then there are certain other processes regulatory processes to go through. So, we do have some time that this would take and we are hoping that in this interim period there will be something.

Moderator: The next question is from the line of Mahrukh Adajania from Nuvama Wealth Management Limited.

Mahrukh Adajania: Yes. So I had a question, partly linked to Suresh. So, your asset growth for the quarter was just 3% Q-o-Q, whereas you know at the time of the merger or at the Analyst Day, the guidance was achieving 18% Y-o-Y, even on a merge balance sheet basis. Should does that stay? And were there corporate loan exists at the end of the quarter?

Srinivasan Vaidyanathan: So there are two aspects. You touched upon how to think about the loan growth and then we've talked about the wholesale growth at the end of the quarter. The way you think about the loan is not quarter-to-quarter. That is why we give kind of a indication to look back to see how the bank has grown the loan book over a period of time. You can look at a three-year block or a two-year block or a five-year or a 10-year block. Whichever blocks you look at, it would be, call it 2.2 -- every five years, 2.2x or 2.3x, or thereabouts, which is back to 18% to 20%, that is what I think your memory says, because that is the historical thing.

So, quarter-to-quarter there can be variations. But in this quarter, if you see, still it is 19.9% -- 19.5% and the growth of the IBPCs alone grew 23.5% -- 23.6%, I think it was.

So, the loan growth can come and it's a question of on the wholesale that you touched upon. It's a matter of how we prioritize in terms of what we want and at what price. If you look at the wholesale the spreads as such. If you think about the bond spreads in the quarter, the bond spreads widened in the quarter.

And whereas the loan has to come and catch up over time. So, we took a stance saying that, from a pricing point of view we will wait for the price to come up. We don't need to. And so, the wholesale was minus 1%. The bond spreads went up anywhere from 30 to 60 basis points, the market bond spreads widened.

So, we do have to wait and see how the loan starts to catch up on the yield from an opportunity point of view. Where the other banks in the country or the financial market participants would appropriately start to price and looking at how the bond spreads are moving. So, it's a question of a quarter-to-quarter timings will be there.

Mahrukh Adajania: But my broader question was that, if you see some of the economies have already downgraded growth forecasts for India. So, what is your sector growth assumption for FY'24? And then of course you would grow above the sector to justify your 17% to 18% year-on-year growth for the next year and then maybe for the next two to three years? So, is it just a tactical call based on pricing? I think there is adequate growth to grow 18% with quarterly variation? Is that a fair assumption?

Srinivasan Vaidyanathan: Yes. It's a fair assumption, it is a tactical thing. We see good demand for loans, more than over INR 30,000 crores, INR 40,000 crores of loans, we did not go through. We didn't want to go because the price has to catch up with what we are seeing on the bond market and it didn't catch up, so we let go.

And we do see good demand in the NBFC segment in the PSU or in the retail and infra segment, we do see good amount of demand coming. And we are also getting on to the new product lines that I mentioned too again driven through PLI or other aspects, we are also into those.

Mahrukh Adajania: So would you have a call on the sector growth rate for FY '24? I mean, any such loan growth?

Srinivasan Vaidyanathan: No, maybe.

Mahrukh Adajania: And sorry, just one follow-up. Basically, what would be the quantum of tax difference INR 350 crores, what would it be?

Srinivasan Vaidyanathan: What is it?

Mahrukh Adajania: Interest on tax?

Srinivasan Vaidyanathan: Yes, six basis points would be approximately INR300 crores, yes. That was it. It is not tax, its interest on tax.

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

Saurabh Kumar: Srini, so three questions. One is, could you comment on what's your revolve rate on the cards business? And your spends have gone up. I just want to see what the revolve rates are? The second is what will be the LCR both for the average and period end? And lastly, just coming back to this NIM, so this cycle, HDFC Bank has shown lower NIM sensitivity versus if I look at your private sector peer group.

So, would it be fair to say, as rates -- if they were to go down maybe in second half of the year, we should again see lower sensitivity on NIMs today? That will be three.

Srinivasan Vaidyanathan: Saurabh, for asking. On the revolve rate, we haven't seen any pickup in revolve rates. So we're still at 65%, 70% of the pre-COVID levels. We don't see a pickup in revolve rate. Actually, this quarter is slightly down by a one percentage point or so, and understandably third quarter normally goes down because we see higher level of card spends that happen due to various festivals and events.

So you will see that there are more transactors into that mix. So, 1 percentage point change doesn't make, but we are not seeing the pickup in the revolve rate. So that is still far lower than what it used to be in the past. So that's one on the revolve rate. Yes, we do, we are confident that the industry will come back, the revolve segment will come back.

But again we analyze that between what we call the occasional revolver who revolves between 1 to 3 months and 4 to 6 months and 6-plus months and so on. But the cream of that would be somebody who revolves 6-plus months, actually that is not moving at all, it is not.

And you will see that somebody, 1 to 3 months going up or down a bit, but that is again more temporary that happens in this not revolving happens. So, we're not seeing that yet. The second aspect that you touched upon is the LCR. I think, I did allude to 113% LCR in the quarter, so that's close to average EOP, whatever you call it, the 113% of the LCR. You asked about the net interest margin in the context of in the second half, what happens when the rate moves?

See, you can think about our net interest margin over the last three years. Go back to before the rates started to go down. And during the kind of a COVID period or in the current period last year to year and half period. If you look at it, it operates normally between the 3.94 to 4.4, 4.5. And the function of the NIM going up or down, it's about the mix of products. More retail composition in the portfolio gets you higher NIM and comes with higher cost and also comes with higher credit costs such credit cost can come with a slight lag.

So that's the model in which it operates. And otherwise, the cost of funds or the yield, other than the lead and lag effect will move more or less. Quarter-to-quarter some variation, because of the lead and lag effect. But otherwise, it is pretty tight from a match to mix, point of view. So, if the rates were to go down in the second half and it would be the -- still will continue to manage the net interest margin in a stable manner around that historical range.

Moderator: The next question is from the line of Hardik Shah from Goldman Sachs. Please go ahead.

Rahul Jain: Yes, Srini. This is Rahul Jain on behalf of Hardik. Two, three questions. Number one, again coming back to deposit growth. I mean for the whole industry itself; the growth is not really showing any acceleration and banks and all have kind of increase the rates. There is clearly pressure from alternate channels. So do you want to hazard a guess as to the banks need to touch the savings rate also in this in the next couple of months to push on the deposit mobilization?

Srinivasan Vaidyanathan: I do. I certainly don't want to take a guess, but that is you know that that has been something that over a longer period of time has remained more or less within a small range. So that's not something that generally has happened, but again, the way that we don't lead with this. But will follow the leader on that front. But still you know that we priced slightly above than the largest bank player in the country on the savings.

Rahul Jain: So, I mean, what measures can banks take or eventually the loan growth have to take a knock, because the CD ratios are don't have much of a scope, I mean, it can still go up by couple of percent. But how will you all kind of manage the whole growth versus deposit dynamics?

Srinivasan Vaidyanathan: See the growth of deposits, one, of course, the market itself grows at certain rate. And the goal is to grow faster than the market to gain the share. So, like for example, our share is slightly under 10% and gross at call it 80 to 100 basis points in the last year. And similarly, over a five-year period, you would see that it's about 400 plus basis points market share gains.

So that's -- and we strive to get that by expanding our distribution to get closer to the customer with a better relationship. So that's it is all about getting the customer in and deepening that relationship, it takes 21 to 24 months for the customer maturity cycle to peak.

And so you want to get the customer in and work with the customer to get that the maturity to be peaking. That's the only thing. And with the market share slightly under 10%, so it's a long runway to go and get that.

Rahul Jain: Understood. The second question is on the cost side. So, you opened about close to let's say 700 branches in this quarter. How many more you would want to open let say in this quarter and whatever cost that are to accrue with regards to branch expansion, has that already reflected in the numbers or will be some spillover into the fourth quarter as well? Plus, of course, whatever you will open up in this quarter in terms of branches?

Srinivasan Vaidyanathan: Yes. The branches that we intended to open call it 1,500 to 2,000 branches, we probably will open. And in the pipeline, we have at least another 600 odd branches in the pipeline to go. And then we keep adding into that. Again, it's not a function of whether we know which locations and how many we want to open. It's a question of getting the least consummated in an appropriate manner and getting the fitment done on time. It's just a function of that.

So yes, we are pursuing that branch build strategy and we have little more than 600 in the pipeline to go, in the shorter time period, it will come. From a cost point of view, those cost will mostly come in the following quarter and to the extent that it goes into later part of the quarter, then the cost will mostly spill into the following year itself, because the cost maybe a month or less than a month type of cost and then it will goes through. So from a cost point of view, it also depends on the timing on that.

Rahul Jain: Let's just maybe one more. On the priority sector, did we do any buyouts in this quarter? How are we placed on that front? Because the growth is remaining strong and any update from RBI on the potential exemption that we applied for the merger?

Srinivasan Vaidyanathan: No, we haven't heard as I was saying that we would expect at some point in time, maybe there is the 27th NCLT meeting and from then on there are a few other regulatory things to go through, before the effective date and maybe in the interim period there will be next year. So there is no target date or a timeframe set on that, and we hope to hear as soon as possible on that.

But on the other question that you asked, in terms of the priority sector, yes, we do buy in the market, different products, one is to do with the core growth, which is a significant push. The core PSL growth is about 35% up year-on-year. So that the total loan is about 19.5% year-on-year and the core PSL, which means the on books PSL that we originate and has grown at the rate of 35%, so far, that's one.

So that means, it gives good ROA and that is the priority and that is the push. And then there are other opportunities that we go and tap too, which is the PSLC or the IBPC or the RIDF, which is again that's a continuous evaluation that happens between the alternative cost of various such strategies and then that is how we use that.

Rahul Jain: But do we have any significant shortfall out there or we are okay, I mean, with growth picking up in the core PSL book?

Srinivasan Vaidyanathan: The shortfall or excess gets determined more at the end of the year in terms of how we do and that is where it comes, but if you look at what we have done over the past several years, typically, the overall PSL, it's 40%. That's certainly we are always there and even now we are there, in the mid-40s plus. It's a question of how do we get to the right kind of a composition on the agricultural and the micro.

These are the two things that you focused to get there. And which we always endeavor a look for organic growth because it is tough to get organic growth. And then where we can't get, we go to the market to see how we can get PSLC or IBPC. And even if that doesn't work, we evaluate whether RIDF is another choice on to that. So all of these get worked and normally it is an annual type of a target and goal.

Rahul Jain: Can I squeeze in one more small question if you don't mind, on consumer behavior, our lending has been strong, the personal lending, personal loans, growth has been strong quarter on quarter. But we see their inflation continues to remain high, the EMIs have gone up. So how do you think about this portfolio shaping up over the next couple of quarters?

Asset quality seems to be strong, but do you think growth may take some knock because of these factors or we are seeing some revolver shifting to the EMI loans, which one is getting clubbed here? So just wanted to understand how this piece is going to evolve over the next couple of quarters?

Srinivasan Vaidyanathan: So we still see quite an amount of -- that's part of their retail spend, if you see retail card spend if you see, almost 27% retail card spend growth, which is quite good. Similarly, if you look at the acquiring business spend that was also in the 20s, good robust acquiring. So you are seeing people are spending. I'm talking about this quarter. That is happening. And another thing, if you see, there is enough liquidity also there with the kind of a customer, I'm talking about our customer base.

If you take our cards customer base, I think last time I alluded to and it is true now too, which is the card customer liability balances in the bank is over five times. So that means if there is 100 of our card receivable balance at an aggregate level, the deposits from that bunch of customers is like five times that? So that mean -- and pre-COVID, I think it was, we said, it is less than three and half times or four times. So people have built up liquidity and it seems to be there, among our customer base. And we do see good amount of spend happening.

Rahul Jain: So that should continue, even the personal loan book should continue to grow. It's what I understood?

Srinivasan Vaidyanathan: You've seen the personal loan book in the quarter grew close to mid-20s, like 24% or something you've seen growing. Similarly, even the sequential growth you're seeing good amount of sequential growth even on the personal, yes, 6% sequential, 23% year-on-year on the personal loan, you're seeing that growth.

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

Nitin Aggarwal: Hi. Srini, I have two, three questions. Firstly, if you can provide some color on the credit card acquisition strategy? We recently talked about like doing 1 million cards per month. How are you planning to achieve this and the timeline for it?

Srinivasan Vaidyanathan: One, we acquired 1.2 million cards in the quarter. And I don't think we have said 1 million per month if anything that's more of a strategic call. But I can tell you that we are at about 1.2 million in this quarter and the prior quarter was slightly under 1 million for the quarter. That's the kind of rate at which we are acquiring cards.

Nitin Aggarwal: This was there in the media very recently, so I thought of clearing this. But no worries. Secondly, like this quarter we have consumed small amount of contingent provisions. So what is your approach to utilization of these provisions going ahead?

Srinivasan Vaidyanathan: See every quarter as we have said in the past, we evaluate what to do and if there is a kind of a minor release, it happens, or a build that happens. But broadly, if you think about how to think about it, which is also I think one of the notes we have given the COVID, one of the important kind of drive that we build the reserves and even before COVID, we built on certain another economic considerations. I wouldn't say that is all behind us.

So if you look at certain markets, in the East of the country or in the West of the country, the covid cases are far higher, far, far higher and it's spiking. And I am not wishing that we follow what we followed last time with a lag of three or four months, I'm not wishing, but we got to be watchful to see how that turns out. So we keep evaluating how this turns out and that's all we keep the provisions on books.

Nitin Aggarwal: Right. And lastly on the liability, this quarter we have reported like a pretty strong TD growth almost 6% Q-on-Q. So can you share some color as to what has been the mix of savings deposits, which have moved to TDs or alternately when you talk about INR 67,000 crores of retail deposits. So, during the quarter, what will be the mix of SA and term in these incremental deposits?

Srinivasan Vaidyanathan: So, I think, mix of both, given you the savings account growth, I think, it's about 13-odd percent in the quarter. Time deposit growth is about 27% or so. The current account growth year-on-year is 8%. But however, I did mentioned that the retail current account which is the granular current account, which is a big focus for us is at 14% year-on-year growth, however the wholesale current account de-grew by 4% in the quarter.

So the CASA ratio is 44%. The long-term CASA is about 40% or 39%, 40% in the long term. And if you think about the time deposit last year FY'22, the whole year the time deposit grew by only 7%. So it's a question of the customer preference and the rate cycle that happens and that's all the growth, and I gave you the rate of growth across each one of these products.

Nitin Aggarwal: Sure, Srini. I will work that out.

Moderator: The next question is from the line of Kunal Thanvi from Banyan Tree Advisors Private Limited.

Kunal Thanvi: So I had two questions. One was the employee addition. Can you throw some light on the breakup of employee addition in terms of branch related and others? And within others, what are the areas where we are adding employees? Because last nine months we have added around 25,000 employees, how much work to do with new branches and how much is non-branch?

Srinivasan Vaidyanathan: See, the most of the staff additions will be in frontline. Frontline means either they are in retail asset sales, which entails because you know that after a couple of years of slowdown we did pick up, so retail asset sales. Branches also adds in out of the 30 odd thousand, more than call it 60 odd percent would be simply directly branches. And then when I say assets, it is both cards and retail assets, both of them would also be there as part of the growth.

So yes, we have about, call it 84% or so of our people in the customer facing role, that's where most of the -- in some manner or the other, I gave you two, three examples of liability branch products or asset sales product or a card sales type of product. But that's the kind of growth where in the frontline handling the customer in some manner or the other, either in relationship management or in sales, that's where predominant growth come from.

Kunal Thanvi: Sure. And the second question was on, if you look at our fee income, the share of credit cards and payment products have been gone to 34% for this quarter. So can you throw some light on how the contribution of fee and payments have been improving? And what's the outlook there? What is that sustainable number one should look at?

Srinivasan Vaidyanathan: Again, it depends on yes, the payment business was 32% of the total fees last quarter, 33%, in this quarter. So it is more or less in that kind of it. And normally in the third quarter you would expect that it contributes slightly higher than what it used to contribute historically. And last year third quarter was an aberration because of certain other things I alluded to at that time from a coming-off the restructuring. A lot of these risk-related type of fee, where people check bounce fees or the late payment fees or the over credit limit fees, et cetera, et cetera.

They all came down, because they are all risk-related fees. And with the curtailment of all of those last year in the COVID period, they were down. But otherwise, there is no particular outlook I can give, it's a function of customer behavior on these things. But yes, it has gone up from 32% composition to 33% here, and again depends on the seasonality and the promotions we run period-to-period.

Moderator: The next question is from the line of M.B. Mahesh from Kotak Securities.

M.B. Mahesh: Hi, Srini. Okay. If I were to just ask one clarification. What is the accounting treatment of IBPC? And when HDFC mortgage book customers who had to come down to your bank, how does the pricing of those loans move? Because they have a different interest rate regime and banks have a different interest rate regime.

Srinivasan Vaidyanathan: On the accounting literature, I think it's in a public document somewhere in terms of what that is and we can take it offline or one of our finance team can talk to you to, to show you where it is. So it's a very simple thing, you'll see.

M.B. Mahesh: Sir, in the sense, do we have to move to EBLR or do they have a choice to continue where they are?

Srinivasan Vaidyanathan: This is on the mortgage, you are talking about, right?

M.B. Mahesh: Absolutely.

Srinivasan Vaidyanathan: Your second aspect of the question in terms of the mortgage. There will be a one-time change that we will do when the migration happens. We are working through that my integration process, and once it integrated, we'll exactly communicate with the customer how that will move. And then of course at any point in time customers have a choice. Even today they have and in future they will have a choice to pick the external benchmark or whatever they need.

M.B. Mahesh: So just on the first question then, on the IBPC part. Does that increase in sale of loans through IBPC, have any impact on the NII or the fee income line?

Srinivasan Vaidyanathan: There will be NII depending on whether the IBPC is done at a price above the cost of funds or below the cost of funds and so on.

M.B. Mahesh: Correct.

Srinivasan Vaidyanathan: And similarly there will be some impact on the IBPC. Yes.

M.B. Mahesh: And how was it this quarter, if I had to ask that?

Srinivasan Vaidyanathan: IBPC will have some impact, so if you look at our loan growth, 19.5%, growth of IBPC, the loan growth is 23.5%.

M.B. Mahesh: On the NII line?

Srinivasan Vaidyanathan: On the NII line there will be some impact. It could be at any point in time, could be 0 to 5 basis points or 10 basis points at any time.

M.B. Mahesh: And if you can give a clarification, what is the definition of a retail current account?

Srinivasan Vaidyanathan: So retail current account is the customers managed out of the branches. Wholesale customer is normally a big corporate or a wholesale customer relationship managed, whereas in a branch managed, that is what we call the retail. Example, it could be a merchant around the corner somewhere or it could be certain another institution, which the branch is managing and opening and maintaining that account.

Moderator: The next question is from the line of Pranav Gundlapalle from Bernstein Private Wealth Management.

Pranav Gundlapalle: Just a quick question on the NIM. You explained how the change in loan mix is driving the change in NIMs, so that's clear. But within a given segment, have you seen a change in your risk footprint over last two, three years, which can also explain, at least part of that linkage? Then if we look in personal loans, going to add safer segments or would the corporate going to add safer segments, anything you see of that sort play out?

Srinivasan Vaidyanathan: Pranav, your line is echoing, I didn't get it all. I know the question is about the NIM from two, three years and something, but I didn't get it exactly. If you can slowly repeat, I'll try to.

Moderator: Pranav, if you're wearing any headphones or earphones, we would request you to speak to the handset directly.

Pranav Gundlapalle: Okay. I'll please try it once again. My question was, you explained about how change in loan segment, explained the change in NIM that you've seen. Is there a change in relative riskiness of the between the segment itself? Have you seen a shift to a safer or less risky segments within personal or any particular segment?

Srinivasan Vaidyanathan: I got it. You are asking about the relatively, of course, yes, absolutely, because the change in our composition that we saw when the wholesale moved from 45% to 55%, from a total composition, we did see a significant improvement in the quality of the customer. These were very highly rated corporates. Our wholesale customers, wholesale book is at about an average internal rating, call it about 4.3 or so is equivalent to AA rating, yes, the quality of the book.

And one other thing is also it comes with a lower risk weights, anywhere from 20%, 30% and retail comes to the 100% risk weight. Yes, it comes with a different type of risk metrics. And that is why, when the wholesale comes, it will come with a lower margin, cost to income which is very low, virtually no marginal cost to income. And credit cost, our experience on the credit cost has been that you will see that hardly any credit cost that we report on this segment. So whereas on the retail, come with a higher margin, higher cost of origination, higher cost of maintenance.

It will come with the credit cost; credit cost can come with a lag too. So that's part of the model. But one thing is from a returns point of view, if you think about the returns, more or less they will be matching, from a ROA, you will see that, call it approximately 2% could be 2.1%, 1.9%, but approximately 2%. Irrespective of the segment in which we operate, we manage to optimize the ROA, because if the margin is low, cost is low, credit cost is low. And so you get to the margins and get to the returns that you want to get. That's how we manage that. And so over a period of when the shift has happened, you see that the ROA remains pretty stable.

Moderator: Ladies and gentlemen, we have come to an end of the time allocated for the call. I would now like to hand the conference over to Mr. Vaidyanathan for closing comments.

Srinivasan Vaidyanathan: Thank you, Tanvi, and thank you to all the participants for joining in today. Any further questions, comments or anything, the team is available and at some point in time we can connect over the next few days. Thank you. Have a great weekend. Bye-bye.

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