Equity Research

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BSE Sensex: 59307

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Q2FY23 result review and earnings revision

Banking

Target price: Rs 2,451

Earnings revision

(%)	FY23E	FY24E
PAT	↑ 7	↑ 4

Shareholding pattern

	Mar '22	Jun '22	Sep '22
Promoters	26.0	26.0	26.0
Institutional investors	57.5	57.8	57.8
MFs and other	9.3	9.0	9.0
FIs/Banks	0.1	0.1	0.1
Insurance Cos.	7.0	8.0	8.0
FIIs	41.1	40.7	40.7
Others	16.5	16.2	16.2

Source: BSE

ESG disclosure score

Year	2020	2021	Chg
ESG score	33.9	33.9	-
Environment	3.5	3.5	-
Social	14.3	14.3	-
Governance	83.6	83.6	-

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, I-sec research

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INDIA

Kotak Mahindra Bank

BUY
Maintained

NIMs surge, growth benign; credit cost and MTM hit modest, partially offset by elevated opex

Rs1,903

Kotak Mahindra Bank's (KMB) Q2FY23 earnings demonstrated its upbeat stance on repricing benefit, advance growth and credit cost outlook. Factors driving earnings beat include surge in NIMs to 5.17% (up 25% QoQ), advance growth of 25% YoY/5% QoQ, treasury hit being contained at Rs0.63bn and modest credit cost of 26bps. This was partially offset by opex rising 10% QoQ/28% YoY. Endeavour to accelerate the liability engine may exert some deposit cost pressure. Building in credit growth of 23%, and estimating NIMs, RoAs/RoEs at >4.8%/2.3%/13%, respectively, we maintain BUY on the stock with an unchanged target price of Rs2,451 (4.15x FY24E book value). Key monitorables: 1) Ramp up in retail liabilities; 2) succession planning related to MD and CEO retirement in Dec'23.

What surprised positively

- Risk-adjusted growth approach evident in 5% QoQ / 25% YoY advance growth primarily led by retail, particularly credit card, BL/PL/CD, retail MFI, home loans, SME, business banking and CVs.
- Loan repricing benefit (53% EBLR linked and 16% MCLR linked advances), asset mix change (deployment of liquidity for growth and sequential outperformance of unsecured lending) pushed NIMs higher by another 25bps QoQ to 5.17%.
- Slippages were contained at 1.2% and credit cost trajectory too settled at 26bps (excluding covid and restructuring provision reversal).

What was not encouraging

- Having 64% of its investment portfolio in AFS/HTM with a modified duration of 1.05 years led to a further treasury knock of Rs0.63bn (over and above Rs8.57bn in Q1FY23).
- Customer acquisition (2.1mn in Q2), retail asset rollout, investment in technology and future growth weighed on cost pressures with opex rising 10% QoQ / 29% YoY. Cost to assets settled high at >3% and cost to income at >49%.
- Deposit growth continues to lag (up 2.8% QoQ / 11.5% YoY) expanding the C/D ratio beyond 90% and pulling LCR down to 119%.

What to expect for FY23

- Nominal credit cost trajectory makes it comfortable to scale up unsecured retail lending to early-mid teens (from 8.7%). Further levers are available for SME, business banking and corporate lending to gather pace driving advance growth.
- Loan repricing benefit (EBLR with 3-month reset / MCLR with 6-month reset) to flow in coming quarters as well though to be offset by deposit cost pressure.
- Scale up of unsecured retail, technology and franchise investment to keep cost structure elevated. Credit cost to normalise to 40-60bps from <30bps levels.
- KMB's investment portfolio has repriced to current yield levels through MTM knock, but carries the risk of another hit in the event of further rise in interest rate expectations.

Market Cap	Rs3778bn/US$45.6bn
Reuters/Bloomberg	KTKM.BO/ KMB IN
Shares Outstanding (mn)	1,985.7
52-week Range (Rs)	2211/1642
Free Float (%)	74.0
FII (%)	40.7
Daily Volume (US$'000)	62,647
Absolute Return 3m (%)	5.7
Absolute Return 12m (%)	(11.2)
Sensex Return 3m (%)	6.7
Sensex Return 12m (%)	(1.4)

Year to Mar (Stand)	FY21	FY22	FY23E	FY24E
NII (Rs bn)	153	168	214	252
Net Profit (Rs bn)	70	86	105	122
EPS (Rs)	35.1	43.2	52.7	61.6
% Change YoY	13	23	22	17
P/E (x)	41	33	27	23
P/BV (x)	4.4	3.9	3.4	3.0
P/ABV (x)	4.6	4.0	3.5	3.0
GNPA (%)	3.3	2.3	2.0	2.0
RoA (%)	1.9	2.1	2.3	2.3
RoE (%)	12.4	12.6	13.5	13.8

- **Surge in NIMs, 5% QoQ advance growth, modest credit cost lead to earnings beat:** KMB's Q2FY23 standalone PAT (banking business) PAT surpassed I-Sec and consensus expectations growing 27% YoY/25% QoQ to Rs25.8bn. Factors driving the beat include surge in NIMs to 5.17% (up 25% QoQ), advance growth of 25% YoY/5% QoQ, treasury hit being contained at Rs0.63bn and modest credit cost of 26bps. This was partially offset by opex rising 10% QoQ/28% YoY.

  Advances growth of 5% QoQ helped it register YoY growth of 25% (in line with expectations) – growth was led by retail, particularly credit cards, BL/PL/CD, retail MFI, home loans, SME, consumer banking. Corporate banking came off 2% QoQ, flat YoY. NII grew better than expected at 27% YoY/9% QoQ with >25bps QoQ rise in NIMs to 5.17% (53% EBLR linked loans, deployment of excess liquidity and asset mix change). Having 64% of investment portfolio in AFS/HTM with 1.05 years of modified duration led to further treasury knock of Rs0.63bn. Given the investment in technology and roll-out of retail products, operating expenses further gathered pace growing 10% QoQ/>28% YoY. Opex to assets, thereby, settled at >3%. Operating profit grew 14% YoY and 28% QoQ.

  Slippages were contained at 1.2%, though technical with one-third getting upgraded in the same quarter. Credit cost was a mere 26bps (excluding utilisation of covid buffer of Rs440mn).

- **Non-banking businesses contributed ~28% to consolidated earnings:** Consolidated profit was up 31% QoQ / 21% YoY to Rs36.1bn. Auto financing business profitability retraced to Rs2.22bn (after contracting to 1.57bn in Q1FY23 from Rs3.13bn / Rs2.5bn in Q4 / Q3FY22 and Rs8.9bn for FY22). Life insurance profitability sustained at Rs2.7bn (Rs2.48bn / Rs2.67bn / Rs2.5bn / Rs1.6bn in Q1FY23 / Q4 / Q3 / Q2FY22). Earnings momentum in capital market related business improved a tad sequentially, including Kotak Securities at Rs2.24bn and KMIL at Rs780mn (vs Rs630mn QoQ). However, Kotak AMC at Rs1bn sustained trajectory, while KMCC's profit was down to Rs220mn. Overall, KMB reported consolidated RoA of 2.61% and RoE of 14.1%.

- **GNPAs declined 16bps to 2.08%; slippages contained at 1.2% with one-third getting upgraded intra-quarter:** GNPA decline was better than expected at 2.08% (from 2.24%/2.34%/2.71%/3.15%/3.56% in Q1FY23 / Q4 / Q3 / Q2 / Q1FY22, 3.25% in FY21). Slippages during the quarter were contained at Rs9.83bn (1.2% annualised run-rate *vs* 2.0% / 1.1%), though one-third (Rs3.3bn) got upgraded during Q2FY23 itself. This was reflected in recoveries and upgrades of Rs9.45bn. There was no sale to ARC during the quarter. Restructuring pool stands at Rs9.9bn (Rs3.53bn of covid + Rs6.4bn of MSME restructuring) compared to Rs10.76bn / Rs12.05bn / Rs13.6bn in Q1FY23 / Q4 / Q3FY22 – 34bps of advances (*vs* 38bps / 44bps). It has created additional provisioning of Rs2.07bn on the same. SMA2 outstanding was further down to Rs1.19bn (Rs1.6bn / Rs1.9bn / Rs3bn / Rs3.9bn in Q1FY23 / Q4 / Q3 /Q2FY22) – 4bps of advances. KMB is getting more confident on credit risk having sailed through the covid second wave relatively well and the management highlighted it is going through the most benign credit cycle ever.

- **Credit cost at 26bps; utilised Rs440mn of covid buffer:** Credit cost during the quarter was a mere 26bps, lower than our expectations (*vs* 0.16% / 0.27% / 0.35% / 0.63% / 1.33% in Q1FY23 / Q4 / Q3 / Q2 / Q1FY22) excluding covid buffer reversal. KMB dipped further into covid provision to the extent of Rs4400mn in

Q1FY23. Covid provision now comes down to Rs4.38bn. Provisioning coverage improved to 73.7% (*vs* 72.6% / 73.2%) and net NPAs were contained at 0.55% (lower than the pre-covid average of 0.7-0.9%). This needs to be considered in conjunction with standard provisioning (Rs12.7bn) + covid-related buffer of Rs4.38bn (17bps of advances) and Rs2.07bn provisioning on the restructured pool. Considering FY22 and Q1FY23 trend, we are building in credit cost of 0.4% 0.6% for FY23E/FY24E, respectively. Kotak Mahindra Prime's net NPA contracted to 1.3% (1.5% / 1.7% / 2.1% / 1.8% / 2.4% in Q1FY23 / Q4 / Q3 / Q2 / Q1FY22).

- **NIMs surged 25bps QoQ to best-ever levels of 5.17%:** Currently, 53% of advances are EBLR (repo-linked), 16% MCLR-linked, 9% fixed-rate with tenure of <1 year and 22% fixed rate with >1-year tenure. Management highlighted that EBLR loans have 3-month reset period while MCLR loans would be repriced with 6-month reset. Loan repricing benefit, asset mix change (deployment of liquidity for advances growth and sequential outperformance of unsecured lending – namely credit card, PL/BL/CD and retail MFI) led to surge in NIMs by 25bps QoQ to 5.17%. Banking business NII growth settled much better than expected registering 27% growth YoY, 9% QoQ. The benefit of further upward revision in EBLR and MCLR is yet to fully reflect in NIMs. With modest growth in deposits, endeavour is to accelerate the liability engine, too, so it may exert some deposit cost pressure.
- **Treasury knock contained at Rs630mn despite higher AFS/HFT book:** KMB had taken trading and MTM hit of Rs0.63bn in Q2FY23 (*vs* Q1FY23: Rs8.57bn, Q1FY22: Rs2.74bn, Q4FY22: Rs3bn; FY22: Rs11.6bn). Proportion of AFS+HFT book is as high as 64% dominated by the fixed-income book (Rs500bn). Modified duration of AFS +HFT is 1.05 years. There has been some churn in the investment portfolio that restricted the treasury knock.
- **Upbeat on advance growth; sequential momentum was broad-based across all segments except corporate advances:** Standalone advances were up 5% QoQ. On a higher base YoY, loan book grew 25% (vs 28% / 21% / 18% / 15% / 6.6% YoY in Q1FY23 / Q4 / Q3 / Q2 / Q1FY22). Growth (YoY) was more broad-based across all segments; sequential momentum too was led by credit card segment (up 16% QoQ/81% YoY), PL/BL/CD (up 13% QoQ/82% YoY), retail MFI (up 22% QoQ/120% YoY) along with home loans rising 6% QoQ/40% YoY, SME growing 9% QoQ/25% YoY and consumer banking scaling up 7% QoQ/22% YoY. Proportion of unsecured retail advances (including retail microfinance) inched up to 8.7% (vs 7.9% QoQ / 5.8% YoY) and, with credit cost being contained at low level, it is comfortable scaling up unsecured lending to mid-teens going ahead. CV financing, too, registered 6% QoQ increase (up 26% YoY).

  Bank is focused on quality customer acquisition, strengthening market share and consolidating relationships for cross-sell. It is getting more constructive on unsecured lending (PL, credit card, MFI) with better ability to analyse data. Almost the entire sourcing of credit cards was from its existing customer base of assets and liabilities. KMB has significantly enhanced capacity for sales / services and is revamping its risk models and analytics setup for a better credit evaluation process. Corporate banking, too, was down 2% QoQ / flat YoY as it continues to remain selective given the irrational pricing by some of its peers. However, credit substitute soared 16% QoQ/28% YoY now constituting 8.5% of customer assets. With a constructive approach towards unsecured lending and levers available to grow

SME, business banking and corporate banking, we believe the bank is well positioned to grow at 23% / 20% for FY23E / FY24E, respectively.

- **Deposit traction still moderate with 2.8% QoQ / 11.5% YoY growth:** KMB has been at the forefront to have deposit rates hiked both for term as well as saving deposits. Term deposits exhibited 8% QoQ growth with retail TD constituting 67% of term deposits. Current deposits were up 13% YoY / 5% QoQ despite the fall in custodian balance. On the contrary, saving deposits were down 3% QoQ due to lumpy withdrawals by some HNI and affluent clients given better returns in liquid funds. Given the increase in savings deposit rate, average cost of savings deposits inched up to 3.8% (vs 3.59%/3.52% /3.74%). Bank's endeavour is to accelerate its deposit engine through 1) deeper engagement with retail customers, 2) aggressively tapping NTB customers, and 3) building institutional (including government) business and scaling up salaried customer base. With deposit growth lagging advance growth, C/D ratio surpassed 90% (*vs* 88.5% QoQ / 80% YoY) and LCR was pulled down to 119%.

- **Cost to assets settle high over 3.0%:** Overhead costs were up 35% YoY / 4.4% QoQ) due to technology spend and push for advance and deposit growth. Cost of building unsecured retail as well as customer acquisition through 811 app is upfront and reflected in the elevated cost. Rising rates saw a small benefit on employee cost. Nonetheless, sharp rise in dearness allowance has driven employee cost higher by >20% YoY as well as QoQ. Overall, we are building in opex to assets at 2.9%/ 3.0% for FY23E/FY24E, respectively.

Table 1: Non-banking businesses now account for ~25-30% of consolidated earnings

(Rs mn, year ending March 31)

Particulars	Q2FY23	Q2FY22	YoY Growth (%)	Q1FY23	QoQ Growth (%)	FY21	FY22	YoY Growth (%)
Kotak Mahindra Bank	25,810	20,320	27	20,710	25	69,648	92,083	32
Kotak Mahindra Prime	2,220	2,400	(8)	1,570	41	5,340	9,450	77
Kotak Mahindra Investments	780	890	(12)	630	24	2,580	3,620	40
Kotak Mahindra Life Insurance	2,700	1,550	74	2,480	9	6,920	4,460	(36)
Kotak AMC and TC	1,060	970	9	1,060	-	3,460	4,080	18
Kotak Securities	2,240	2,430	(8)	2,190	2	7,930	9,830	24
Kotak Mahindra Capital	220	580	(62)	510	(57)	830	1,840	122
International subsidiaries	50	270	(81)	140	(64)	1,540	970	(37)
Others	640	130	392	440	45	1,010	820	(19)
Total	**35,720**	**29,540**	**21**	**29,730**	**20**	**99,258**	**1,27,169**	**28**
Affiliates & Others	370	350	6	(2,180)	(117)	660	(1,380)	(309)
Consolidated PAT	**36,080**	**29,890**	**21**	**27,550**	**31**	**99,918**	**1,25,789**	**26**

Source: Company data

Table 2: Upbeat on advance growth; sequential momentum was broad-based across all segments

(Rs mn, year ending March 31)

Customer Assets (Rs mn)	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	YoY %	QoQ %
Home Loans & LAP	6,14,790	6,88,710	7,60,770	8,09,750	8,58,430	39.6	6.0
Consumer Bank WC (Secured)	2,30,790	2,40,800	2,64,440	2,63,910	2,81,810	22.1	6.8
PI, BL & Consumer Durables	72,610	85,540	1,00,710	1,17,120	1,31,970	81.8	12.7
Credit Cards	43,630	49,480	55,720	68,190	79,030	81.1	15.9
CV/CE	1,94,810	2,03,880	2,24,900	2,32,460	2,46,040	26.3	5.8
Agriculture Division	2,10,540	2,26,000	2,52,000	2,46,040	2,50,020	18.8	1.6
Micro Finance	96,200	1,01,280	1,07,660	1,10,150	1,20,150	24.9	9.1
Tractor Finance	20,210	24,000	30,600	36,500	44,440	119.9	21.8
Corporate Banking	6,53,570	6,80,950	6,66,740	6,66,330	6,55,240	0.3	(1.7)
SME	1,77,780	1,89,940	2,04,440	2,05,290	2,23,100	25.5	8.7
Others	34,550	38,770	44,560	45,970	50,000	44.7	8.8
Total Advances	**23,49,480**	**25,29,350**	**27,12,540**	**28,01,710**	**29,40,230**	**25.1**	**4.9**
Credit Substitutes	2,13,880	2,16,340	2,12,270	2,34,580	2,73,010	27.6	16.4
Total Customer Assets	**25,63,360**	**27,45,690**	**29,24,810**	**30,36,290**	**32,13,240**	**25.4**	**5.8**

Source: Company data

Table 3: Valuation of subsidiaries

Particulars - Rs mn	Valuation basis	Total value	Stake	Stake value	Value per share
Kotak Life	**2.25x Appraisal value**	2,74,651	100%	2,74,651	138
Kotak Prime	**2.0x PBV**	1,79,680	100%	1,79,680	91
Securities / Investment Banking	20x PE	2,56,499	100%	2,56,499	129
MF/Offshore/AUM/PE	6.0% of AUM	2,29,238	100%	2,29,238	116
Total					**474**

Source: Company data, I-Sec research

Kotak Mahindra Life Insurance: PAT grew 74% YoY/9% QoQ to Rs2.7bn

- Gross written premium for Q2FY23 grew 11.5% YoY. Individual APE NB premium for Q2FY23 grew 13.7% vs private industry growth of 7.0%. Overall, protection premium for Q2FY23 grew 54.1% YoY.
- AUM (policyholders') as of Q2FY23 stands at Rs537.85bn, up 13.8% YoY.
- Death claims net of reinsurance amounted to Rs2.75bn (Q2FY22: Rs5.54bn mainly due to covid-19 claims).
- Company with net worth of Rs47.92bn has solvency ratio above the regulatory requirement at 2.79x vs 2.72x QoQ and 2.61x YoY.

Table 4: Kotak Life Insurance - key metrics

(Rs mn, year ending March 31)

Particulars	Q2FY23	Q2FY22	YoY Growth (%)	Q1FY23	QoQ Growth (%)	FY21	FY22	YoY Growth (%)
New Business premium	32,500	29,150	11	22,580	44	1,11,010	1,30,150	17
Profit After Tax	2,700	1,550	74	2,480	9	6,920	4,260	(38)

Source: Company data

Kotak Mahindra Prime: Car advances up 21% YoY; earnings up 41% QoQ on low base

- In Q2FY23, earnings were adversely impacted by Rs1.11bn of one-time charge due to change in accounting related to brokerage (up-fonting unamortised brokerage charge in Q1). On a low base, Q2FY23 earnings were up 41% QoQ to Rs2.22bn.
- NPA fell to 1.3% vs 1.5% QoQ and 1.8% YoY.
- Car advances were up 21% YoY / 8.7% QoQ. Management indicated robust outlook for car financing demand, especially the mid and upper end cars. The demand for lower-end cars is relatively gradual leading to inventory pile up.
- Company remains healthy with capital adequacy of 30.1% *vs* 31.0% QoQ and 30.6% YoY.

Table 5: Kotak Mahindra Prime - key metrics

Rs mn	Q2FY23	Q2FY22	YoY Growth (%)	Q1FY23	QoQ Growth (%)	FY21	FY22	YoY Growth (%)
NII	4,210	3,450	22	4,170	1	12,330	14,570	18
PBT	2,980	3,200	(7)	2,100	42	7,210	11,790	64
PAT	2,220	2,400	(8)	1,570	41	5,340	8,860	66
Auto Advances	2,04,000	1,68,450	21	1,87,730	9	60,030	60,930	1
RoAA	3.2	4.0	(20)	2.3				

Source: Company data

Kotak Securities: Market share improved QoQ to 5.1% led by cash segment

- Kotak Securities reported PAT of Rs2.24bn (up 2% QoQ and down 8% QoQ) with market share rising QoQ to 5.1% (*vs* 4.3%). Market share in cash segment was 11.2% vs 10.4% QoQ and 11.0% YoY.
- It has launched new age trading platform “Kotak Neo” - faster, simple, seamless trade experience. Company’s plan is to shift majority or all trading volumes into smart Neo over the next 9-12 months.
- Digital highlights - 354% YoY growth in Internet Trading ADV and 493% YoY growth in Mobile Trading ADV.

Table 6: Kotak Mahindra Securities - key metrics

(Rs mn, year ending March 31)

Particulars	Q2FY23	Q2FY22	YoY Growth (%)	Q1FY23	QoQ Growth (%)	FY21	FY22	YoY Growth (%)
Revenues	6,310	6,130	3	6,160	2	20,190	25,010	24
PBT	2,980	3,250	(8)	2,910	2	10,570	13,340	26
PAT	2,240	2,430	(8)	2,190	2	7,930	10,010	26
PAT margin (%)	35	40		36		39	40	

Source: Company data

Kotak Mahindra AMC - PAT of Rs1.06bn, flat QoQ

- Earnings of Kotak Mahindra AMC were flat QoQ at Rs1.06bn (PBT at Rs1.43bn).
- It launched equity NFO ‘Kotak Business Cycle Fund’ in Sep-22 wherein it collected Rs 22.7bn.
- Equity (Ex-ETF & Arbitrage) AAUM market share was 6.31% in Q2FY23 vs. 6.04% YoY.
- Monthly SIP inflows remain healthy which stood at Rs7.8bn for Sep’22 (vs Rs7.3bn in Jun’22 and up 26% YoY).
- Company has been launching active as well as passive funds

Table 7: Domestic asset management business - key metrics

(Rs mn, year ending March 31)

Particulars	Q2FY23	Q2FY22	YoY Growth (%)	Q1FY23	QoQ Growth (%)	FY21	FY22	YoY Growth (%)
PBT	1,430	1,300	10	1,430	-	4,640	6,010	30
PAT	1,060	970	9	1,060	-	3,460	4,550	32
Average AUMs	28,41,490	27,05,120	5	28,38,850	0	23,47,980	28,64,780	22

Source: Company data

Table 8: Q2FY23 result review (standalone)

(Rs mn, year ending March 31)

Particulars	Q2FY23	Q2FY22	% Change YoY	Q1FY23	% Change QoQ
Net Interest Income	**50,994**	**40,206**	**26.8**	**46,970**	**8.6**
% Growth	26.8	3.2		19.2	40.0
Fee income	17,600	14,190	24.0	16,560	6.3
Add: Other income	1,950	3,930	(50.4)	(4,120)	(147.3)
Total Net Income	**70,544**	**58,326**	**20.9**	**59,410**	**18.7**
% Growth	20.9	9.4		12.2	
Less: Operating Expenses	34,861	27,130	28.5	31,575	10.4
Pre-provision operating profit	**35,683**	**31,196**	**14.4**	**27,835**	**28.2**
Loan loss provisions	1,810	3,850	(53.0)	880	105.7
Other provisions	(440)	390	(212.8)	(644)	(31.7)
PBT	**34,313**	**26,956**	**27.3**	**27,599**	**24.3**
Less: taxes	8,498	6,642	28.0	6,885	23.4
PAT	**25,807**	**20,320**	**27.0**	**20,712**	**24.6**
% Growth	27.0	(7.0)		26.1	
Balance sheet (Rs mn)					
Advances	29,40,232	23,49,650	25.1	28,01,710	4.9
Deposits	32,52,032	29,17,111	11.5	31,64,830	2.8
Asset quality					
Gross NPL	62,102	76,580	(18.9)	63,786	(2.6)
Net NPL	16,304	24,914	(34.6)	17,493	(6.8)
Gross NPL ratio (Change bps)	**2.08**	**3.19**	**(111)**	**2.24**	**(16)**
Net NPL ratio (Change bps)	0.55	1.06	(51)	0.62	(7)
Credit cost (Change bps)	0.19	0.73	(55)	0.03	15
Coverage ratio (Change bps)	74	67	628	73	117
Business ratio					
			Change bps		**Change bps**
RoA	2.38	2.02	36	1.94	44
RoE	13.6	12.2	137	11.3	234
CASA	56.2	60.6	(444)	58.1	(195)
Credit / Deposit Ratio	90.4	80.5	986	88.5	189
Cost-Income ratio	49.4	46.5	291	53.2	(373)
Tier I	21.5	22.8	(130)	21.2	30
Earnings ratios					
			Change bps		**Change bps**
Yield on advances (Calculated)	8.91	8.15	76	8.21	71
Cost of deposits (Calculated)	3.61	3.20	41	3.25	36
NIM (Reported)	**5.17**	**4.45**	**72**	**4.92**	**25**

Source: Company data

Kotak Mahindra Bank: Q2FY23 earnings call takeaways

Mr. Uday Kotak's remarks and commentary

- ***Presently, the bank is in the most amazingly benign credit cycle, very closely linked to terminal rates and inflationary pressure***
- ***Credit growth – significant growth seen in CV, tractor, microfinance, SME, unsecured retail, home loan***
- Loan growth is quite solid and improvement in mix of unsecured retail (including MFI) which is now 8.7% of total lending book. ***Looking at this number to mid-teens which is where bank is comfortable going to***
- ***As interest rates move up, 70% of book is floating. Of the balance 30%, 10% is less than 1 years***
- Very high focus on granular deposits – easy customer engagement, digitally acquiring customers, salaried customer base that's more steady
- ***Investment book duration is less than 1 year - Modified duration of AFS +HFT is 1.05 years.*** *64% of book which is* ***MTM and HTM book*** *is around 35% of total investment book*
- ***CA*** - wherein growth was about 13% YoY despite fall in custodian balance. Monitoring and measuring granular SA book, particularly SA balance upto Rs1mn which is showing continuing growth during this period
- High SA balance saw some withdrawals by High NW and affluent customers due to higher returns in liquid funds
- TD which is other than CA and SA has grown pretty well
- ***Subsidiaries performance*** continues to be good except for a few which were impacted by volatility in capital markets

Margins

- *Margins rise due to external benchmark linked loan profile and unsecured share rising in loan mix among other factors*
- ***Larger part of the book is linked to Repo and hence banks are being benefited on the yields side. 53% of advances are EBLR (repo linked), 16% MCLR linked, 9% fixed rate with tenor of <1 years and 22% fixed rate with more than 1 year tenor.***
- *Margins at 5.17% vs. ~4.5% a year ago.* Also, margins would depend on loan mix wherein bank is inching high yielding unsecured retail and microfinance share in total loan book.
- On deposits, 56% (CASA) is fixed rate book since CA rate is nil and SA is quasi-fixed rate book

- Unsecured retail is growing faster than the rest of the book which is also aiding margins
- *Industry is probably in one of the most important cindrella time in terms of credit growth cycle*
- *Interest rate cycle and margin cycle looks pretty benign as of now*
- *Overall, company is very focused on risk adjusted returns*

Liabilities

- ***Upward revision in interest rate cycles has led to high investments by HNI in TD or liquid funds***
- Granular SA book which is below Rs1mn has seen good demand
- Good traction seen in agency business which will help build flows and balance in CASA accounts
- Launched couple of saving products to garner deposits
- CASA at 56% and CRAR at 22.6% including H1 profits and CET at 21.5%. LCR at 119.1%.
- ***TD less than Rs 20mn would be ~67% of total term deposits***

Digital

- ***Mr. Milind has joined as CTO - he comes from a very strong background and has global banking experience***
- *Added new Chief of Customer Experience*
- Aim is to build resiliency as bank grows its customer base and builds scale
- Working on creating scale and capacity to meet future needs on payments and transactions side
- ***Transitioning to cloud over the next 9-12 months except core banking***
- Launched face authentication, first in the industry
- ***MOBILE has become the biggest branch today. Hence, large number of projects and investments going in Do It Yourself (DIY) journey and assistance towards the same.***

Asset quality

- ***Slippages include Rs 3.3bn which were upgraded during the same quarter***
- Restructuring at 0.34%
- SMA 2 for exposure over Rs 50mn at Rs 1.19bn

Opex

- There was a tad reversal in employee cost due to movement of G-Sec yield. Despite this, there was an increase in employee cost due to sharp rise in DA
- Will continue to steadily add branches, however density requirement of branches would be less now as compared to earlier years in this new digital era
- Highest delta in overhead cost is technology and digital cost. Also upfront customer acquisition cost due to roll out of retail products.
- Running projects to reengineer and optimise processes through technology.

Advances

Wholesale and SME banking

- SME segment - growth remained robust - YoY 23% and QoQ 9%
- Seeing good demand for capacity creation in the form of term loans which get utilised over time
- ***Continue to grow and gain market share in SME with ultimate aim of being holistic banker to this segment of customers***
- Corporate book - advances growth was flat while credit substitutes growth was up 16% QoQ
- ***Corporate book - there is fair amount of pricing irrationality and hence remain choosy***
- ***Commercial Real estate - LRD pricing remains irrational and hence bank has relatively stayed out of this market***
- DCM fees have moderated while all other fees continue to grow at robust pace
- Integrated banking portal is gaining good traction among customers
- Non-custody CA growth remains robust. On custody, domestic custody remains good.
- ***Credit substitutes built this year are all 1-year instrument. For credit substitutes with longer duration, they are on floating basis.***

Commercial vehicle

- Strong demand in Q2
- ***Bus segments has bounced back and doing well***
- Will look to build book with focus on risk adjusted returns
- Collection efficiency improves for this segment
- Construction equipment - good demand in September after muted July and August
- Tractor finance - seen an uptick in demand after better cashflows
- Bank has improved market share in tractor financing

- Continue to remain focused on rural customers in farmer segment
- CV segment has come back after past 2 tough years.
- Car finance is growing 18-20% in volume and value growth of 25%
- Dealer inventory building at lower end but mid-range and premium segments moving very fast

Agriculture

- Commodity charges have peaked in Q1 and seen little reduction in commodity prices in Q2
- Capex investments in this segments are seeing an uptick
- Warehouse, cold storage, supply chain seeing good demand

Consumer business

- ***LAP seeing good demand***
- Mortgage business up 29% YoY
- ***Acquired 725k cards during the quarter***
- Spends up 93% YoY
- Credit card advances were up 60% YoY

Subsidiaries

Kotak Mahindra Prime (KMP)

- ***Value growth at 25% in YoY industry, though volume wise it is 18% YoY***
- ***Demand for lower end cars is stable, but mid and upper end cars is moving at a pretty fast pace***
- KMP customer asset base of >Rs200bn

Insurance

- ***PAT of Rs2.7bn, up 74% YoY and 9% QoQ***
- GWP at Rs 32.5bn, up11.5% YoY
- Individual new business APE up 13.7% vs. pvt industry growth of 7% YoY
- Protection premium up 54.1% YoY (combination of more life cover and higher rate of protection premium being charged which also aids profitability to a certain extent)
- Rs 530bn AUM

- ***Death claims now normalised to pre-covid levels***
- Rs 47.92bn NW with solvency ratio of 2.79

Kotak Securities

- Revenue at Rs 6.3bn
- PBT Rs 2.98bn vs Rs 3.25bn YoY
- ***PAT at Rs 2.24bn vs. Rs 2.43bn YoY and Rs 2.19bn QoQ***
- Cash market share at 11.2% vs. 11.0% YoY an 10.4% QoQ (seeing steady share)
- ***Options volume driving overall market volumes with ADV of Rs 64.7trn of which options is Rs 63trn vs. Rs 30trn YoY***
- Significant uptick in digital journey wherein it has launched Kotak Neo in previous quarter
- Plan is to shift majority or all trading volumes into smart Neo over the next 9-12 months

Kotak AMC

- ***Equity AUM up 6% to Rs 1.52trn despite market volatility***
- ***SIP flows remain healthy***
- ***Equity market share at 6.1%***
- Retail AUM stands at 53%
- ***Continue to serve investors by having active as well as passive funds***
- ***PAT flat at Rs 1.06bn***
- ***Total AUM up 2% YoY at Rs 3.9trn***

Kotak Mahindra Bank: Q1FY23 earnings call takeaways

Mr. Uday Kotak's remarks and commentary

- ***The word 'CHANGE' is the new comfortable feeling at Kotak***
- ***Outlook -depends on how commodities cycle plays out globally.*** USA FED goes upto3.5% by CY22-end and every central bank is following suit
- ***As of yesterday, liquidity stood at Rs8.08trn vs. Rs 1.29trn as of June 2021 For the short term, Indian interest rates will tighten in his view.***
- ***Asset book for fixed rate less than 1 year + floating rate is more than 80% of advances which is consistent with macro view that short-term interest rates will inch up. More than 1-year loan fixed rate loans is only 20% of total book***
- ***EBLR reset is done every 3 months and MCLR reset is done every 6 months***
- ***Credit cost at 4bps annualised and without covid write-back and restructuring, it will be 16bps***
- Overall continue to be quite confident of building loanbook and ***is comfortable scaling up unsecured lending from 7.9% of advances to early-mid teens.***
- Quite comfortable and confident of growing deposit franchise along with it.

Investment book

- Duration on non-HTM book at 1yr
- Overall fixed income book at Rs880bn of which 39%is HTM and balance Rs500bn is AFS+HFT with duration of 1 yr
- Hit on P&L of Rs8.57bn due to rise in g-sec yield
- ***On 31st March 2022, 1-year treasury bill yield was 4.45% and on 30th June 2022, it wat 6.2%***
- ***Bank has not transferred any book to HTM in Q1***
- ***Even in September 2013, bank had a very high MTM number but entire was taken upfront and not amortised***

Asset quality

- GNPAs decline to 2.24% (from 2.34% in Q4).
- ***Slippages during the quarter were Rs14.4bn offset by recoveries and upgrades of Rs13bn. Of the slippages, Rs7.8bn got upgraded within Q1FY23 itself.***
- Credit cost during the quarter was 16bps excluding covid buffer reversal.
- It dipped further into COVID-19 provision to the extent of Rs650mn in Q1FY23. COVID-19 provision now comes down to Rs4.8bn. No sale to ARCs

Fee income and opex

- Rising rates saw a small benefit on employee cost
- Non-employee cost increased due to advertisement/promotion, technology spend and push for advance and deposit growth

Loanbook and Deposits

- Advances book up 29% YoY
- ***Retail unsecured book which includes microfinance is at 7.9% and is comfortable scaling it up to early–to-mid-teens.***
- Corporate loan book growth was moderate lower due to irrational pricing in few cases.
- ***Continue to look at 15-20% in corporate and 25% growth in SME segment***
- ***Invested significantly in bank's platform***
- When there is pricing pressure, it looks more towards credit substitute
- Increase in Q1FY23 in credit substitute was towards short term duration.

CV finance

- Saw good growth YoY
- Disbursements were considerably higher YoY
- Decent reduction in fuel prices is helping operator economics
- PV business is almost back to normal
- Demand for CE continues to be good
- Tractor industry continue to grow YoY as well as QoQ and bank continues to grow its market share

Retail lending

- All retail lending product saw good demand
- Mortgage - continue to see demand for home loans
- Acquired 0.6mn cards, which is best-ever
- Bulk of sourcing is from existing products
- Consumer finance – good quarter across physical and digital distribution
- WC and business banking – seen focus on growth and focus on prime quality
- Continue to grow retail MFI book. Collection of demand in this segment has also been good
- Demand for capex has been increasing and seen increase in
- 85% of business banking portfolio qualifies for PSL
- ***Will see upfront acquisition cost and tech cost higher for the next 1-2quarters***

Deposits

- Focus continues to be on growing granular deposits
- CASA at 58.1%. ***CASA and TD below Rs50mn comprise 88% of deposits***
- Bank had 34.5mn customers, up 28%YoY
- Built a very low base of government business and will continue to focus on growing the same. Till now, bank was completely absent from govt business but with announcement in past budget, now private banks are also being able to participate.
- NR segment ATS for SA deposits at Rs400k-500k
- For retail, SA ATS would be under Rs100k
- Cost of SA at 3.59%
- ***SA rates - Upto Rs5mn is 3.5% and above Rs5mn is 4% (50bps higher than larger banks)***
- ***On TD rates, difference is ~10bps when compared to large banks***

Digital initiatives

- Will focus on continuously improving digital infrastructure
- Will focus on wholesale as well as corporate side
- Key digital metrics as outlined in presentation are Mobile banking app
- 98% of SA transaction volume are in digital or branch mode

Credit cards

- EMI has grown more than revolve rates and EMI rate is in-line with industry
- Revolve rates is 30%, which is in-line with industry
- ***Close to 100% of credit card sourcing is from internal assets and liabilities customers***
- Year ago revolve ratio was 27% and now it is 30%

Consolidated performance

- Rs27.55bn PAT, up 53% YoY
- Rs.37trn - customer assets
- Capital adequacy at group level >20%
- Book value at Rs502/share
- Cons. RoE at 11.2%
- Bank contributed 70% of total PAT including subs (Banks PAT is 26%higher YoY)

Kotak Securities

- Mkt share has grown during the quarter
- Franchise remains strong

- Continues to gain new account opening market share
- Institutional business Research Analyst and Sales continues to be highly rated
- PAT at Rs 2.19bn

Kotak Mahindra Prime

- Rs 1.57bn PAT
- Rs1.11bn one-time charge due to change in accounting related to brokerage.
- ***Sourcing of car is through brokers and earlier expense was amortised, but now it has been taken upfront. Also, whatever was unamoritsed until FY22 has now been taken into P&L.***
- Demand for cars continue to be good despite rise in car prices

Kotak AMC

- SIP inflows up 34% YoY to Rs 7.3bn
- Continue to serve investor requirement by launching active as well as passive funds
- Rs1.06bn PAT
- Total AUM across at Rs3.78trn, up 10% YoY

Miscellaneous

- 34.5mn customer base
- ***Average LCR for the quarter was 119.9%***
- Focused on risk adjusted margins and this will drive bank's behaviour
- Revolve rate is 30%; EMI has grown reasonably and faster than revolve

Chart 1: Upbeat on advance growth; sequential momentum was broad-based

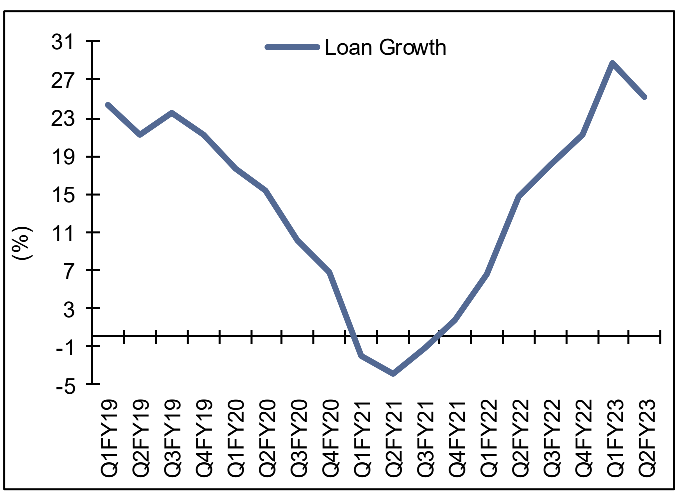
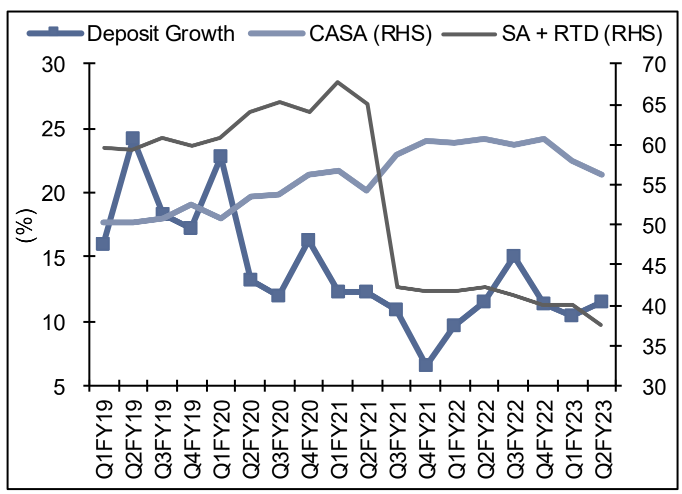


Chart 2: Deposit traction still moderate with 2.8% QoQ / 11.5% YoY growth



Source: Company data, I-Sec research

Chart 3: NIMs positively surprised expanding further to 5.17%

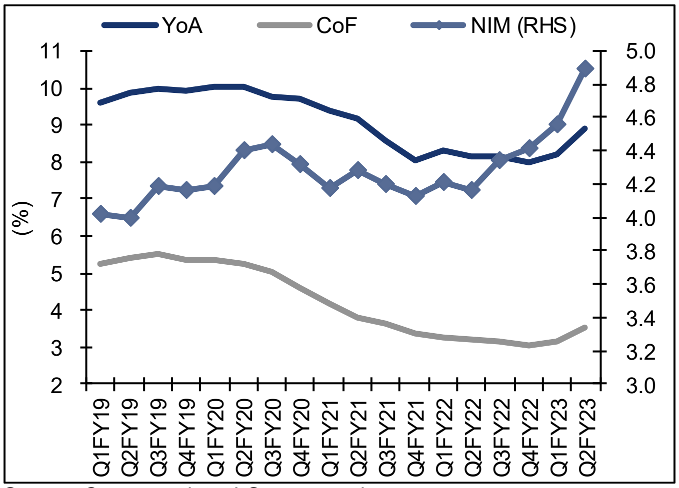
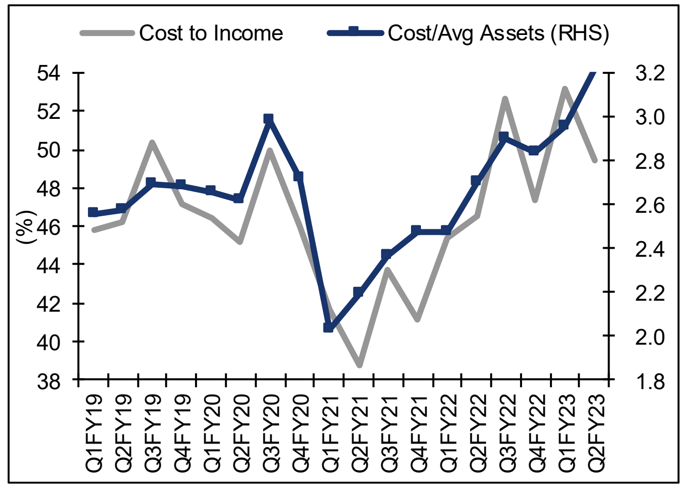


Chart 4: Cost to assets settle high over 3.0%



Source: Company data, I-Sec research

Chart 5: GNPAs declined 16bps to 2.08%; slippages contained at 1.2%

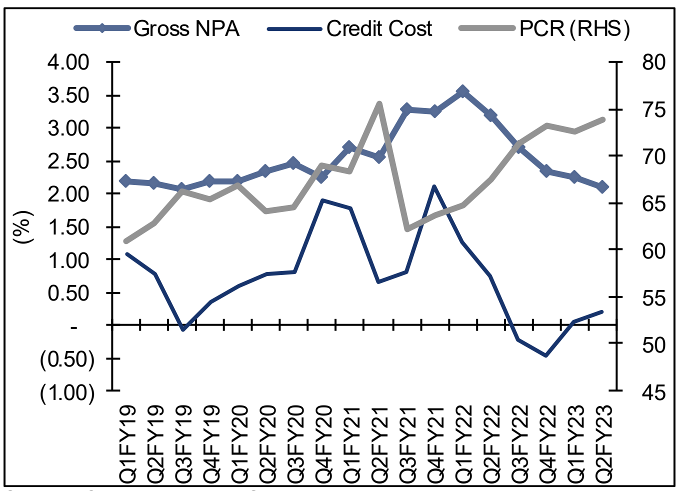
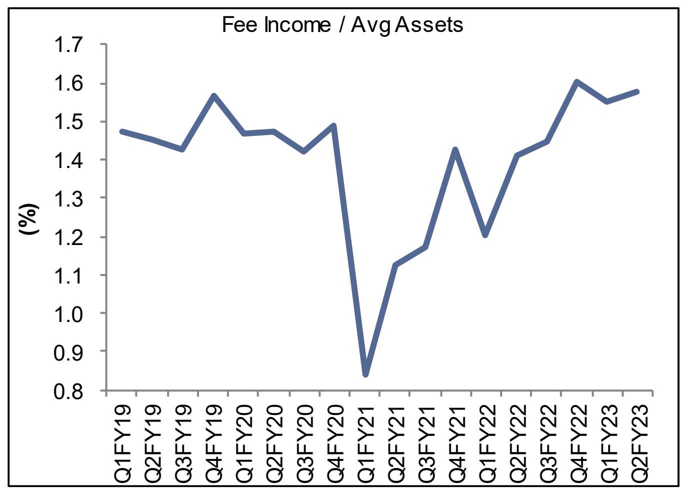


Chart 6: Fee income retraces a bit from higher levels



Source: Company data, I-Sec research

Chart 7: RoA range-bound

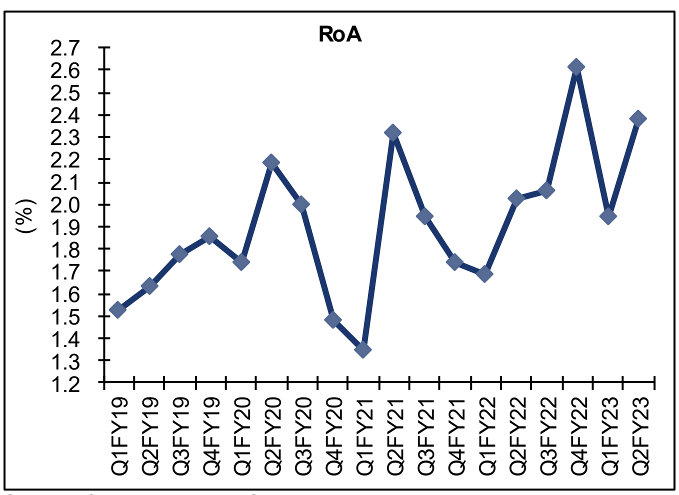
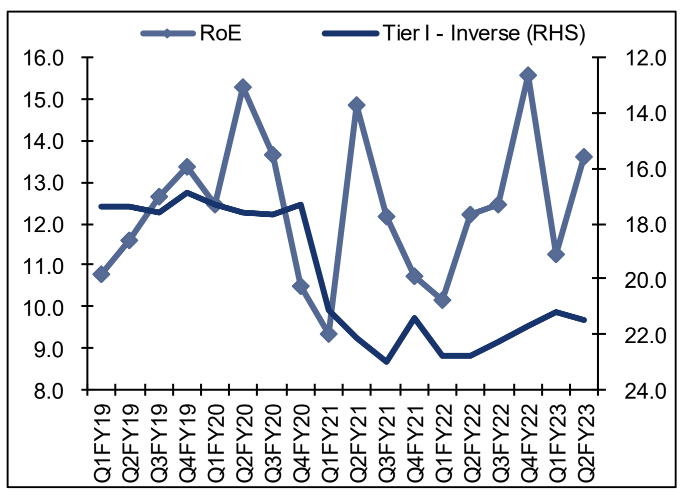
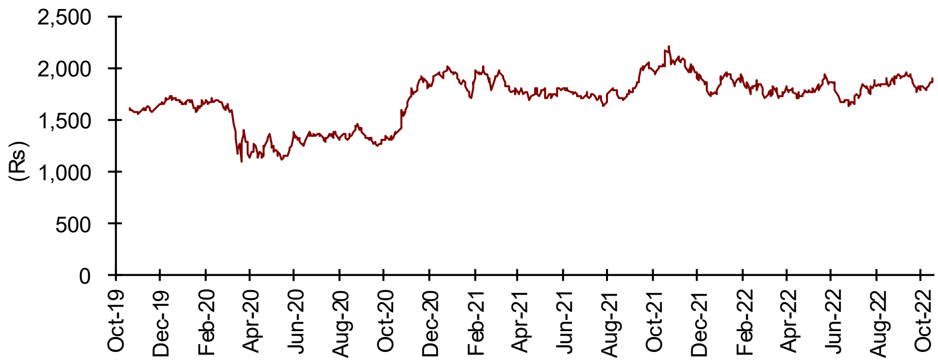


Chart 8: Capital adequacy strong



Source: Company data, I-Sec research

Price chart



Source: Bloomberg

Financial summary (standalone)

Table 9: Profit and loss statement

(Rs mn, year ending Mar 31)

	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Net Interest Income	**81,261**	**95,317**	**1,12,590**	**1,34,997**	**1,53,397**	**1,68,179**	**2,14,391**	**2,51,629**
% Growth	18	17	18	20	14	10	27	17
Fee income	21,207	27,645	33,908	37,793	34,000	45,000	54,900	68,625
Add: Other income	13,565	12,877	12,132	15,929	20,460	18,544	18,796	26,059
Total Net Income	**1,16,033**	**1,35,839**	**1,58,630**	**1,88,718**	**2,07,856**	**2,31,723**	**2,88,087**	**3,46,313**
% Growth	22	17	17	19	10	11	24	20
Less: Operating Expenses	(56,185)	(64,257)	(75,148)	(88,509)	(85,841)	(1,11,214)	(1,35,351)	(1,59,179)
Pre-provision operating profit	**59,848**	**71,582**	**83,482**	**1,00,208**	**1,22,015**	**1,20,509**	**1,52,736**	**1,87,134**
NPA Provisions	**(6,144)**	**(6,248)**	**(8,442)**	**(14,760)**	**(19,029)**	**(15,130)**	**(9,673)**	**(20,396)**
Other provisions	(2,223)	(3,151)	(1,182)	(7,401)	(9,956)	8,234	(3,173)	(3,295)
PBT	**51,481**	**62,182**	**73,858**	**78,047**	**93,030**	**1,13,613**	**1,39,889**	**1,63,443**
Less: taxes	(17,366)	(21,339)	(25,205)	(18,575)	(23,382)	(27,886)	(35,210)	(41,139)
PAT	**34,115**	**40,843**	**48,653**	**59,472**	**69,648**	**85,727**	**1,04,679**	**1,22,304**
% Growth	63	20	19	22	17	23	22	17

Source: Company data, I-Sec research

Table 10: Balance sheet

(Rs mn, year ending Mar 31)

	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Capital	9,204	9,528	14,544	14,565	14,909	14,923	14,923	14,923
Reserve & Surplus	2,66,975	3,65,310	4,14,460	4,75,617	6,22,382	7,09,955	8,11,377	9,30,425
Deposits	15,74,259	19,26,433	22,58,804	26,28,205	28,01,000	31,16,841	35,84,367	42,29,553
Borrowings	2,10,955	2,51,542	3,22,483	3,79,933	2,36,507	2,59,671	2,83,588	3,09,897
Other liabilities	84,507	96,521	1,11,430	1,04,197	1,60,088	1,92,894	2,12,183	2,33,402
Total liabilities	**21,45,900**	**26,49,334**	**31,21,720**	**36,02,517**	**38,34,886**	**42,94,284**	**49,06,440**	**57,18,201**
Cash & Bank Balances	2,25,720	1,96,201	2,46,755	5,32,923	3,96,265	4,29,239	3,43,392	3,84,141
Investment	4,50,742	6,45,623	7,11,891	7,50,515	10,50,992	10,05,802	10,86,266	11,94,893
Advances	13,60,821	16,97,179	20,56,948	21,97,482	22,36,886	27,12,536	33,49,198	40,17,719
Fixed Assets	15,376	15,272	16,516	16,231	15,353	16,437	22,505	24,914
Other Assets	93,240	95,059	89,611	1,05,365	1,35,390	1,30,269	1,05,079	96,533
Total Assets	**21,45,900**	**26,49,334**	**31,21,720**	**36,02,517**	**38,34,886**	**42,94,284**	**49,06,440**	**57,18,201**
% Growth	11.6	23.5	17.8	15.4	6.5	12.0	14.3	16.5

Source: Company data, I-Sec research

Table 11: DuPont analysis

(%, year ending Mar 31)

	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Interest income	8.7	8.2	8.3	8.0	7.2	6.7	7.2	7.5
Interest expense	(4.7)	(4.3)	(4.4)	(4.0)	(3.1)	(2.5)	(2.6)	(2.8)
NII	**4.0**	**4.0**	**3.9**	**4.0**	**4.1**	**4.1**	**4.7**	**4.7**
Other income	0.7	0.5	0.4	0.5	0.6	0.5	0.4	0.5
Fee income	1.0	1.2	1.2	1.1	0.9	1.1	1.2	1.3
Total income	**5.7**	**5.7**	**5.5**	**5.6**	**5.6**	**5.7**	**6.3**	**6.5**
Operating expenses	(2.8)	(2.7)	(2.6)	(2.6)	(2.3)	(2.7)	(2.9)	(3.0)
Operating profit	**2.9**	**3.0**	**2.9**	**3.0**	**3.3**	**3.0**	**3.3**	**3.5**
NPA provision	**(0.3)**	**(0.3)**	**(0.3)**	**(0.4)**	**(0.5)**	**(0.4)**	**(0.2)**	**(0.4)**
Total provisions	(0.4)	(0.4)	(0.3)	(0.7)	(0.8)	(0.2)	(0.3)	(0.4)
PBT	2.5	2.6	2.6	2.3	2.5	2.8	3.0	3.1
Tax	(0.9)	(0.9)	(0.9)	(0.6)	(0.6)	(0.7)	(0.8)	(0.8)
PAT	**1.7**	**1.7**	**1.7**	**1.8**	**1.9**	**2.1**	**2.3**	**2.3**

Source: Company data, I-Sec research

Table 12: Key ratios

(Year ending Mar 31)

	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Per share data								
EPS – Diluted (Rs)	19	21	25	31	35	43	53	62
% Growth	62	16	19	22	13	23	22	17
DPS (Rs)	1	1	1	-	1	1	1	1
Book Value per share (BVPS) (Rs)	150	197	225	256	322	365	416	476
% Growth	15	31	14	14	25	14	14	14
Adjusted BVPS (Rs)	144	191	219	250	311	359	410	469
% Growth	14	33	15	14	24	15	14	14
Valuations								
Price / Earnings (x)	77.1	66.7	56.1	46.0	40.7	33.1	27.1	23.2
Price / Book (x)	9.5	7.3	6.4	5.6	4.4	3.9	3.4	3.0
Price / Adjusted BV (x)	9.9	7.5	6.5	5.7	4.6	4.0	3.5	3.0
Asset Quality								
Gross NPA (Rs mn)	2.6	2.2	2.1	2.3	3.3	2.3	2.0	2.0
Gross NPA (%)	35,786	38,254	44,679	50,269	74,255	64,697	67,835	82,195
Net NPA (Rs mn)	1.3	1.0	0.8	0.7	1.2	0.6	0.5	0.5
Net NPA (%)	17,181	16,651	15,444	15,579	27,052	17,372	17,622	20,622
NPA Coverage ratio (%)	52	56	65	69	64	73	74	75
Gross Slippages (%)	1.5	1.3	1.2	1.6	2.4	1.9	1.6	1.5
Credit Cost (%)	0.6	0.6	0.5	1.0	1.3	0.3	0.4	0.6
Net NPL/Networth	6.2	4.4	3.6	3.2	4.2	2.4	2.1	2.2
Business ratios (%)								
ROAA	1.7	1.7	1.7	1.8	1.9	2.1	2.3	2.3
ROAE	13.2	12.5	12.1	12.9	12.4	12.6	13.5	13.8
Credit Growth	14.7	24.7	21.2	6.8	1.8	21.4	23.3	20.0
Deposits Growth	13.5	22.4	17.3	16.4	6.6	11.3	15.0	18.0
CASA	44.0	50.8	52.5	56.2	60.4	60.7	63.0	64.2
Credit / Deposit Ratio	86.4	88.1	91.1	83.6	79.9	87.0	93.4	95.0
Cost-Income ratio	48.4	47.3	47.4	46.9	41.3	48.0	47.0	46.0
Operating Cost / Avg. Assets	2.8	2.7	2.6	2.6	2.3	2.7	2.9	3.0
Fee Income / Avg. Assets	1.0	1.2	1.2	1.1	0.9	1.1	1.2	1.3
Earning ratios								
Yield on Advances	10.5	9.6	9.8	9.9	8.4	7.8	8.3	8.4
Yield on Earning Assets	9.2	8.6	8.6	8.3	7.5	6.9	7.5	7.7
Cost of Deposits	5.6	5.1	5.3	4.9	3.8	3.1	3.4	3.6
Cost of Funds	5.7	5.2	5.3	4.8	3.8	3.2	3.3	3.5
NIM	4.2	4.2	4.1	4.2	4.3	4.3	4.8	4.9

Source: Company data, I-Sec research

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