

Analyst/Investor Conference Call**July 28, 2006**

Moderator

Good evening ladies and gentlemen, I am Sanjay, the moderator for this conference. Welcome to the J&K Bank Q&A conference call. For the duration of the presentation, all participants' lines will be in the listen-only mode. I will be standing by for the question and answer session. I would like to hand over to Dr. Haseeb Drabu of J&K Bank. Thank you and over to you sir.

Dr. Haseeb Drabu

Yeah hi. Just this is an update on our Q1 results for the current fiscal which the board took account of today morning. The broad story essentially is that whatever we had committed in my earlier conference call as well as the first analyst meet, we have by and large met all those commitments and in terms of all the key financial ratios, we are on course so what we had said we would be.

Starting with of course the net profit it is up 29% from 48 crores Q1 last year to 62.39 crores in the current Q1, and this 62.39 crores profit is after having made a provision of 20 crores on that gets ___ which was 5 crores in the Q1 last year. The strategy of looking at J&K as a focus area seems to have paid off very well. Our net interest margins are up from 2.8 to 2.93. Our yield and advances have improved from 8.8 to 9%, and most importantly our cost of deposits has come down from 5.3 to 4.8% compared to Q1 last year, which is effective of better liability management, and the direct impact of the shift in deposits from corporate to retail is that our CASA ratio has improved from 31 to 37%. The fact that CASA deposits have today dropped from 5.3 to 4.8, this perhaps is the only bank today which actually sees a lower cost of deposit in a regime of high and rising deposit rates, so that has aided our bottom line considerably.

The advances growth has been about 18% and quality of assets has improved further. Our NPA levels are down from 1.22 to 0.72 and quite significantly our NPA coverage ratio has increased from 53 in Q1 last year to 72% in this quarter, so the norm that we have set out is that we do an 80% coverage ratio, we are on course for that as well.

Our return on assets has improved and is up to 1.05% from 0.8% and so is the return on average net worth from 11 to 13. So by and large what we are seeing is what we think is a very good performance in all the key fundamentals of the bank, and going forward I think we would continue along with the same lines that we have done except perhaps improve the rate of growth of advances, the reason why we are today under performing this system is because the volumes in J&K are hard to drive up but we have worked out ___ plans to increase that as

well. The break up today remains at you know 65:35, 65% of advances being outside J&K and 35% remaining in J&K.

As far as the investment portfolio goes on the SLR side, there is absolutely no issues, we are insulated from another 25 basis points hike, we are operating today within the provisions that we have provided, 62% of our portfolio is in the ___ category and about 38% is in EFS. The weighted average duration is actually in the ___ portfolio down to 18 months and about 2-1/2 years for the non SLR. Going forward I think this is going to be a major churning in our non SLR portfolio and that is going to be partially funding our advances growth, we have already seen a large pairing down of our non SLR portfolio and we will continue doing that.

On our pricing front in response to the continuous raising of rates by the Reserve Bank, we sometime back increased our lending rates by a 100 basis points, so we have already factored in the rise that happened day before, which announced by the Reserve Bank of India, and in fact we have factored another 25 basis points which may happen till December, so we are adequately covered in that sense and this should help us show better interest margins going forward in Q2 and Q3.

Our capital adequacy ratio is very comfortable at 13% even after we have kind of grown much faster and deposits have not kept pace indicative of the fact that we are burning our capital more efficiently. Even after the requirements of our VI in terms of various risk weightages that they have done for real estate and other sectors, we do maintain a very comfortable ratio and going forward I think we are looking at around 12 to 12.5 capital adequacy ratio at the end of the year. That is about it this opening comment. I will happy to take any questions.

Moderator

Thank you very much sir. We will now begin the Q&A interactive session. Participants who wish to ask questions please press *1 on your telephone keypad. On pressing *1, participants will get a chance to present their questions on a first-in-line basis. Participants are requested to use only handsets while asking a question. To ask a question please press *1 now. Our first question is from Mr. Deepankar Chaudhry from ICICI Securities.

Deepankar Chaudhry

Good evening Dr. Drabu.

Dr. Haseeb Drabu

Hi Deepankar.

Deepankar Chaudhry

Yeah and great numbers.

Dr. Haseeb Drabu

Thanks very much.

Deepankar Chaudhry

Okay just one clarification, first of all it is housekeeping, have you actually staggered the standard assets provisioning or taken all of that?

Dr. Haseeb Drabu

We have taken all of that.

Deepankar Chaudhry

Already.

Dr. Haseeb Drabu

Yeah.

Deepankar Chaudhry

Okay. The second is about the credit growth part, there has been actually a fairly strong sharp slow down.

Dr. Haseeb Drabu

Yes.

Deepankar Chaudhry

And I mean I would like to know how much of this is a part of your deliberate strategy to focus less on outside of J&K and things are not too good in terms of volume growth in J&K now as just as you mentioned.

Dr. Haseeb Drabu

Yes.

Deepankar Chaudhry

How does it look and you know how could you change this?

Dr. Haseeb Drabu

The issue really on credit growth is that we had done a substantial lending to a particular corporation within J&K, and this was year before I mean year last year we had done 500 to about 700 crores to PDC, Power Development Corporation, which was actually in excess of what was the prudential norm and as we moved around we exited that and that has impaired the growth in J&K seemingly, but frankly this is more like you know in accounting **to work as it works** because outside PDC we have done about 27% growth in Kashmir Valley, and we have done exceedingly well in Jammu which is about 28%, we have done very, very

well in Bombay our credit growth is 53%, and Delhi has been slow at 18%. So frankly it is not really that you know we have put the slow down, yes we have focused on better quality credit smaller and with higher margins, which is showing in our you know interest margins.

Deepankar Chaudhry

Right.

Dr. Haseeb Drabu

But it was largely part of one very large advance in the state which actually created the problem, otherwise I think we are today ..., if you accounts for that and normalize it, I think we are growing at about 22% like to like.

Deepankar Chaudhry

Okay and the deposits are growing just ahead of 7% as a result of you know keeping a lid on your deposit cost.

Dr. Haseeb Drabu

Yes absolutely, but the essential fact there is that we have as I have said that you know I am not very happy with the way we have done our liability management, a lot of it was high cost deposits in corporates, so we have exited all that, and we are focusing on retail deposits, my detail deposit growth in J&K is growing at 18%, which is very healthy, but because I have exited very large chunks in Delhi and in Bombay at the corporate deposits it is actually showing as a 7% growth, but when you look at my retail deposit growth, segment wise, then I am growing upwards of 18 to 20% retail growth, which is also showing in my current account saving account ratio, as it is up, and also my cost of deposit has come down sharply.

Raj Gopal

Hello.

Dr. Haseeb Drabu

Yeah.

Raj Gopal

Hello.

Dr. Haseeb Drabu

Yes.

Raj Gopal

Mr. Drabu Raj Gopal here.

Dr. Haseeb Drabu

Yeah hi.

Raj Gopal

Hi, you have given us in your earnings _____ you have given us the amount of demand deposits but not indicated the break up between savings and current?

Dr. Haseeb Drabu

I have given you

Raj Gopal

The absolute number which is around 77 billion, you have not given the split between savings and

Dr. Haseeb Drabu

We can provide that, between savings and current, the split.

Raj Gopal

Yeah, yeah.

Dr. Haseeb Drabu

Okay, I can get you that.

Raj Gopal

Yeah.

Dr. Haseeb Drabu

Current and savings, my savings in Q1 is 5126 crores.

Raj Gopal

Okay, okay and the balance is, right fine.

Dr. Haseeb Drabu

Yeah.

Raj Gopal

Okay, okay sir thank you very much.

Dr. Haseeb Drabu

Thanks.

Moderator

Thank you very much sir. Our next question is from Mr. Arun Malhotra from Smith Management.

Arun Malhotra

Yeah good evening hi. I just wanted to check on the other income that continues to disappoint.

Dr. Haseeb Drabu

Is that so? I thought fee based income is up 27%.

Arun Malhotra

What is the figure can you give me?

Dr. Haseeb Drabu

Our fee income this quarter is 27.2 crores.

Arun Malhotra

Okay.

Dr. Haseeb Drabu

Up from 22.4 now, when you look at it Q1 on Q1, you are missing an important element in our strategy which was evident in Q4, if you see my Q4 numbers it was 52 crores. Now the reason is a large part of my fee based income comes on an annual cycle. So the thing would be that the strategy which we had put in place which we got rich dividends at you know we saw 100% increase year-on-year, does not show in Q1, because the bulk of my payments come from services to the government, investing banking activities, and stuff like that, which will give me annual thing. I do hope to make it quarterly, perhaps from H1 or a little later, because it does create a certain distortion in our growth, which is what you are pointing out.

Arun Malhotra

Sure.

Dr. Haseeb Drabu

But otherwise you know if you look at it from the proportion of total income to a fee base income to total income, we have improved substantially from what we were earlier a year ago from 12% to 20%. So I am so sure if that is disappointing, but I think we also do there but I think in Q4 we gave you an

indication of what the numbers will be for the year end, and so if you were to look at a 52 as the base and do a 30% growth from that, that is what you look at annualized.

Arun Malhotra

Okay.

Dr. Haseeb Drabu

Yeah.

Arun Malhotra

And can you also elaborate on the insurance you know how much were the insurance premiums collected and what is the progress on that front?

Dr. Haseeb Drabu

You see we are ___ in MetLife and you know ___ as well. Insurance we have not actually focused on it to a very large extent, but now I think we are looking at a business worth 50 to 70 crores and our insurance premium commission in Q1 has actually gone up 150%, the numbers are not very significant but the trend is and if you show a 150% increase in 1 year that is an indication of how we are seeing the business. I think we have done only about 20 crores last year and we are ramping it up to minimum of 50 and upwards about 70 crores of business in this quarter. The issue essentially was resting with MetLife, and ___ got its strategy in place but now there is a fairly important change happened with the management of MetLife and they have put a new guy as well, and I think we are now focused on J&K, the MetLife India strategy revolves around JK, so this is the only place where they see that they could actually provide some competition to LIC, so we are going to focus on the insurance in a fairly large manner in the course of this year and by H1 we should have some results to show.

Arun Malhotra

Okay could you also throw some light on the large projects which are due to be commissioned in J&K and the benefit of which will accrue to J&K in the coming year?

Dr. Haseeb Drabu

We have already seen at least 5 of these go on stream, which I had mentioned, the ADB projects have gone on stream, five of them are already there, road projects and stuff like that, and in terms of the power project two very large power projects will now start, Bagihar starts in about 6 months from now, which is going to give us tremendous amount of you know, and the second is in Uri, has been commissioned, both are power projects. It is not so much completion but a lot of construction projects have started for which we are financing the ancillary activities that is why we are you know lets say now we are now doing road projects and you know the rail project is there, ___ project is there, the urban sewage project is there, so all that is now generating a lot of ancillary demand

which is being funded by the J&K Bank, and a lot of stuff is also happening on industrial front in Jammu where **Samba Badi Bhawana Katuwa** Industrial Estates which have got lot of concessions, and we are seeing a very sharp pick up in advance growth of about 30% in Jammu, so that is going to help us in the next 3 years.

Arun Malhotra

Sure and just one last thing on the competitive landscape, could you just throw some light on the number of branches opened by private sector banks or other PSU banks like SB and PNB, in the last 1 year?

Dr. Haseeb Drabu

Yeah well last 1 year we have seen only to one branch of HDFC come up. SBI has not opened anything. PNB has not opened anything at the moment.

Arun Malhotra

Okay.

Dr. Haseeb Drabu

We are expecting ICICI to open one branch in the course, really at the level of that point I don't think that there is competition happening, because even if they are there they are not lending.

Arun Malhotra

Okay.

Dr. Haseeb Drabu

You know so the main competition does come from PNB and SBI in Jammu and some cooperative banks in districts of Baramula, Kupwara and that is it, but I really see only a change in business competition coming in from a different angle that the customer service is much better than you know than us, and people get used to a certain environment of customer service ____ for which we have put in place a fairly rigorous and expensive brand strategy, which is being unveiled on 26th August in our AGM, so that is the thing, and we will hope to improve our customer service and the ambiance of our branches in the next 6 to 8 months and that will give us a certain advantage.

Arun Malhotra

Okay thank you, thanks a lot.

Dr. Haseeb Drabu

Thanks.

Moderator

Thank you very much sir. Participants who wish to ask questions, please press *1 on your telephone keypad. Our next question is from Mr. Madhuchandar Dey from IL&FS.

Madhuchandar Dey

Hello sir, a good set of numbers. Sir, I wanted to ask you what kind of incremental lending have you done in this quarter in the State of J&K and what kind of yields and what kind of deposits have you garnered from the state; although overall there is a slowdown quarter on quarter, but what is the picture in J&K?

Dr. Haseeb Drabu

There is no slow down as and when you look at 17% growth in the state.

Madhuchandar Dey

That is YOY sir, but sequentially I am talking about, what kind of incremental lending has happened in the State of J&K in this quarter?

Dr. Haseeb Drabu

We have done I think about 700 to 800 crores of incremental lending in the valley and we have done about the same amounts in Jammu. So, we are talking about 300 crores of incremental lending in the state.

Madhuchandar Dey

That would be what percentage of your total lending that has happened.

Dr. Haseeb Drabu

That would be about 36% to 37%.

Madhuchandar Dey

Of your total lending?

Dr. Haseeb Drabu

Yeah.

Madhuchandar Dey

Okay, what about deposits on that side.

Dr. Haseeb Drabu

Deposits about 58% is coming in from the state, and in our deposit base we have grown in J&K at about 18%. So a large part of our deposit is coming in fact

incrementally almost 80% of our incremental ____ deposit is coming from the state.

Madhuchandar Dey

And what is the CASA in J&K as on now?

Dr. Haseeb Drabu

55.

Madhuchandar Dey

CASA in J&K, and sir a couple of housekeeping questions. What is your yield on investment for this quarter?

Dr. Haseeb Drabu

Our yield on investment this quarter is 6%.

Madhuchandar Dey

And sir, what is your tier one.

Dr. Haseeb Drabu

Tier one is 12.57, tier two is 0.42, about 13% total.

Madhuchandar Dey

Okay, thank you very much.

Dr. Haseeb Drabu

Thanks.

Moderator

Thank you very much mam. Our next question is from Shashink from Tower Capital.

Shashink

Sir, congratulations on a good set of numbers.

Dr. Haseeb Drabu

Thank you.

Shashink

Sir, I just wanted to understand our brand strategy pertaining to the licenses which are given by RBI and what are you planning by this year end.

Dr. Haseeb Drabu

We have got about 40 branches. We will be about 30 in the course of this year, out of which 25 are in J&K and 5 are outside. So, and we are trying to basically get into areas which are under-banked, which is why we have got a whole number of licenses, the large parts of J&K under banked, so we are trying to increase our footprint in those areas, and going forward as I have said we are unveiling our brand strategy on August 26th, and we are going to go in for ISO 9000 service standards for our branches in two cities of Jammu and Srinagar, which actually account for a large part of our business. So, that would be principally what we are looking at in the course of next six months.

Shashink

Okay. Sir in terms of bulk deposit to the total deposit, what would be the proportion now?

Dr. Haseeb Drabu

Corporate as a percentage of total deposits would still be in the range of about 40%.

Shashink

Compared to last year?

Dr. Haseeb Drabu

Last year was about 60%.

Shashink

Okay. So, you would want to focus on retail segment rather than focusing on this corporate segment to garner your deposits, and what would be the excess SLR right now under this?

Dr. Haseeb Drabu

There is very marginal excess SLR actually, very very marginal. I think it is for you know _____ excess SLR. What was your earlier question you were asking prior to that?

Shashink

You know, the thing is your growth will be funded through deposit growth only right now.

Dr. Haseeb Drabu

No, it will be deposit growth plus what we are releasing out of the non-SLR side, you know. I am trying to constantly pair my non-SLR portfolio down to fund some part of my advances growth, because today my yield on advance is 5.9% and it will even lower in terms of for the non-SLR thing. So, it is not worth my while to continue that on my books, and as you are exiting, we have been exiting for the last one year, we have reduced it from 3000 to think 1200 crores now, and that itself will also fund a large part of my growth. It's deposit plus my thing, I am substituting credit derivatives with credit now. So, that should also improve my margin, though it will not increase my balancing size. So, I am looking at a somewhat total fund flow and fund management principal and I find that this should be a fairly workable strategy.

Shashink

Okay fair enough, great. Thank you.

Moderator

Thank you very much sir. Participants who wish to ask questions, please press *1 on your telephone keypad. Our next question is from Mr. Manish from Motilal Oswal.

Manish

Hello.

Dr. Haseeb Drabu

Yeah hi Manish.

Manish

I just want to know what amount of branches do we have outside of State of J&K?

Dr. Haseeb Drabu

Total branches are 544, and outside branches are about 120.

Manish

You have mentioned 517 in your press release.

Dr. Haseeb Drabu

517?

Manish

Yeah.

Dr. Haseeb Drabu

Just one minute, let me check. Is it 517 now? Yeah it is 514. Yes, it was 514, up to 517 now. That's right. Sorry, my mistake. 517, that is right. About 120 are outside J&K and the rest are within J&K.

Manish

Just wanted some sense on how has been your performance outside the State of J&K, like how much has been your CASA in those branches and what kind of growth are you seeing in deposits, in fact on your cold deposits in those branches.

Dr. Haseeb Drabu

Yeah, you see our presence outside J&K is not really as a strong retail bank, and essentially our focus has been for the last 10 to 15 years has been lending outside. We are in, as I did mention earlier, that we have seen a 50% growth in advances in our western zone which is Bombay, but we have exited a large part of our deposits in these because they were high cost corporate deposits, and while advances growth continues we are doing low margin high volume business outside J&K, but we have now emphasized a lot of our deposit mobilization in J&K, which is showing an improvement in our CASA from 31% to 37%. Obviously the CASA in you know somewhere like Bombay or Delhi is about 18% to 20%, which is why when you look at the weighted average basis it comes down to 37%. My CASA in J&K is about 55%. So that about 20% is what is outside the state, and 54 is within the state, and that gives an average CASA of about 37%. So, that is how it is functioning. Really, if you want to see the strategic shift, it is not so much on the **larger** side, we do continue to lend very aggressively outside J&K, but it is on the liability side, here we are focusing on far greater lends on retail deposits in J&K and also now outside J&K. We are using more and more products outside J&K to get some retail co-business in place.

Manish

Are you getting enough fee income outside the State of J&K?

Dr. Haseeb Drabu

Yes, we are getting a lot of insurance income outside the state. We are also getting some other you know guarantee business and bank guarantees and stuff, we are increasing that part of our business outside the state as well. We are now offering, we have begun to offer to corporates composite package, not just advances but as well as stated things like guarantees and insurance and all that. So, that is going, but frankly the fee-based income will be driven from within the state of J&K because we have an agreement with the government and we collect a lot of bills for them and you know like electricity and telephone, and stuff, and

on that we do earn user charges and we earn quite well. Also, we are now beginning to focus on J&K as a thrust area for insurance income, and that is going to ramp it up. We also have started investment banking thing for the Government of J&K, which is also extending now outside India because a lot of the corporates are coming in to start up projects there. So, we are doing a lot of syndication for all the projects in J&K and the projects are worth 24,000 crores in the next two to three years. So, we should see a lot of income coming which technically speaking from outside the state because you have corporates coming in, like Airtel is coming in with some project, Reliance is coming in with some project, Mahendra is coming with some project. All these guys are getting loan syndications onto us, so we should see an increase in our fee based income.

Manish

Right. Lastly sir, what kind of margins would you be earning outside the state?

Dr. Haseeb Drabu

It would be between 2.4% to 2.5%.

Manish

So it means that within the state it would be around closer to 3%.

Dr. Haseeb Drabu

More than 3%. We are today operating nationally on a quarterly basis at about 3%, we are almost there.

Manish

2.93%.

Dr. Haseeb Drabu

2.93, yes, we would be in the range of about 3.2% or something like that in the state.

Manish

Right, thank you sir.

Dr. Haseeb Drabu

Thanks.

Moderator

Thank you very much sir. Participants who wish to ask questions, please press *1 now. At this moment, there are no further questions from participants. I would like to handover the floor back to Dr. Haseeb Drabu of J&K Bank for final remarks.

Dr. Haseeb Drabu

Alright, thanks very much. I greatly appreciate your interest in the bank, and I just want to reiterate that we are looking at growth in advances of about 25% to 30% year-end. We are looking at about 15% to 17% increase in deposits, but more significantly, we are looking at a compositional shift in advances that will improve our cost of deposits as it has been done in this quarter. Going forward, we had about six months go stop re-pricing of assets downwards, now we have already factored in re-pricing of assets, which should show us better margins in the course of this year. The other thing that I would like to mention is that if you look at our shareholding we have an FII investment of about 32.5% and our cap, which is induced by the Board, was at 33%. Today, the Board of Directors decided to increase the FII cap in the bank from 33% to 40%. So, that should make the stock a little more active, there is not much trading happening. So, I would expect a lot more interest of investors, in fact we have had a lot of investors coming in saying that they would want to invest more, but because of the cap could not do so. So, we have now raised that cap from 33% to 40%. And, we are looking at an end year EPS of about 55 to 57 rupees in the course of this fiscal, and that is all I have to say. Thank you very much.

Moderator

Ladies and gentlemen, thank you for choosing WebEx conferencing service. That concludes this conference call. Thank you for your participation. You may now disconnect your lines. Thank you and have a nice evening.

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