Investor Call: Business Update Call on recent announcement from HDFC Ltd and HDFC Bank”

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Moderator: Ladies and gentlemen, good day, and welcome to an update call on the recent announcement from HDFC Bank Ltd. and HDFC Ltd.

As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal for an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded.

Without much ado, I now hand the conference over to Mr. Keki Mistry – Vice Chairman and CEO of HDFC Ltd. and Mr. Sashi Jagdishan – MD and CEO, HDFC Bank Ltd. Thank you and over to you.

Keki Mistry: Thank you very much and good morning everyone. At the outset, I would like to welcome all of you to this joint call of HDFC Ltd. and HDFC Bank. I have with me my colleagues from HDFC, Renu Karnad and Rangan and Sashi and Srini are there from HDFC Bank. As you are aware, the board of directors of HDFC and HDFC Bank, at their respective meetings held today, have approved an all stock amalgamation of HDFC with HDFC Bank. The amalgamation is subject to the approval of the shareholders of both the Companies, the Reserve Bank of India, the stock exchanges, the Competition Commission, SEBI, IRDA, and all other regulatory approvals as may be required.

Upon obtaining all approvals, the merger will become effective, and shareholders of HDFC Ltd. will receive shares of HDFC Bank in exchange for shares in HDFC Ltd. at the approved share exchange rate. Bansi Mehta and Company and Deloitte Touche India LLP have prepared their joint valuation report, which has been accepted by the respective boards. Bank of America Merrill Lynch Securities and Morgan Stanley provided the fairness opinion on the exchange ratio to HDFC Ltd. and HDFC Bank respectively. According to the scheme, shareholders of HDFC Ltd., as on the record date. will receive 42 shares each of face value of Rs. 1 each of HDFC Bank for 25 shares each of face value of Rs. 2 each held in HDFC Ltd. The equity shares held by HDFC Ltd. in HDFC Bank will be extinguished as per the scheme. As a result of this, upon the scheme becoming effective, HDFC Bank will be 100% owned by public shareholders, and existing shareholders of HDFC Ltd. will own around 41% of HDFC Bank. The outstanding warrants of HDFC on conversion post the effective date will also convert into shares of HDFC Bank based on the aforesaid share exchange ratio.

In the past, the merger would not have been as value accretive as it is at present. The strategic rationale for the proposed merger is as follows:

Over the last two years, there have been certain regulatory changes for banks and NBFC’s, which have considerably reduced the barriers for a potential merger. In 2020, RBI issued guidelines, which laid the roadmap for conversion of large NBFC’s with asset size of over Rs. 50,000 crores into full-scale commercial banks. This has considerably addressed bottlenecks like semi-urban and rural branch requirements RBI further mandated that within a group, just one entity may be engaged in a specific product line. This would require a reassessment of the group structure.

Secondly, RBI has harmonized asset quality reporting between the banks and NBFC's. Thirdly, in addition to the SLR on regulated deposits, HDFC is now also required to maintain a liquidity coverage ratio. Consequently, the gap between the liquidity requirements of a bank and NBFC have considerable reduced. Also, NBFC's are required to move to a core financial service solution platform, which is akin to the core banking solution of a bank. Scale-based regulations could, in due course, further harmonize regulations between banks and NBFC's in future. So, first is on deregulations. Second, is if you look at the CRR, SLR requirements for banks, these have reduced considerably over the years to the current level of 22% of the demand and time liabilities. Also, interest rates are significantly lower today as compared to earlier years and hence the negative carry-on raising funds to meet the CRR, SLR requirements will be considerably lower today.

HDFC currently does not have a priority sector lending requirement and hence, as a part of the combined entity, HDFC Bank would have had to raise funds and increase its PSL requirements through direct lending in the area of agriculture and micro, small and medium enterprises industries. This would have had operational inefficiencies besides resulting in an additional negative carry. This incremental funding would also have carried an additional CRR, SLR requirement. RBI has now permitted banks to hold priority sector lending certificates. These certificates are instruments that enable banks to achieve the priority sector lending targets without actually disbursing those loans.

HDFC has non-convertible bonds of nearly Rs. 80,000 crores, which have an original maturity of over seven years. Subject to RBI approval, these bonds would qualify as affordable housing bonds and consequently would not carry CRR, SLR requirements. Real estate, over years, has seen an increased level of transparency and regulations. Paramount among these are the Real Estate Regulation Act 2016, the insolvency and bankruptcy code, and many other regulations that have been introduced. This has resulted in an increased level of activity by banks in the real estate sector, both retail and wholesale. Mortgages offered by the combined entity can be widely delivered in an efficient and profitable manner. HDFC will benefit from the lower funding costs of the bank and from its very large distribution franchise while HDFC Bank will benefit from HDFC's expertise in the real estate space and its efficient processing of loans, which has enabled an 8.1% cost-income ratio.

The amount invested by HDFC Ltd. in the capital of HDFC Bank currently has to be reduced from HDFC Ltd.'s tier 1 capital for computing the capital adequacy. This has a negative impact on the return on equity and consequently any future infusion of capital by HDFC Ltd. into HDFC Bank to maintain the stake at over 20% would have resulted in a further negative drag on HDFC's ROE. As per our estimate, 70% of the customers of HDFC and its subsidiaries do not bank with HDFC Bank and hence the merger will provide the ability to cross-sell banking products to this very large pool of customers thereby enhancing the overall business of the combined entity. You will observe from the aforesaid that most bottlenecks of earlier years had been largely addressed, and at this stage, the boards of both institutions, after evaluating all options, have decided that this is an opportune time to announce the proposed merger of the two entities for the mutual benefit of all its stakeholders.

The proposed merger will consolidate and leverage the significant from complementaries of HDFC, the largest housing finance company in India and HDFC Bank. It will bolster the capital base and balance sheet of HDFC Bank and make it a very large bank even by global standards. The merger is a coming together of equals and will result in mutual benefit to both the institutions and their stakeholders. This strategic merger will bring economies of scale and enable the combined entity to leverage of each other's strengths. The customer will be the biggest beneficiary. It is estimated that as of date over 70% of HDFC Bank's customers do not have a mortgage. Further, under the combined entity, cross-sell of the group products in insurance, both life and non-life, asset management and pensions will see significant improvements in efficiencies and in profitability.

The proposed merger will dovetail the efficiencies of HDFC as a premium mortgage originator with over 45 years of domain expertise in efficient mortgage processing at a significantly attractive cost-income ratio into the lower cost of funds of the bank and its wide distributing capability. Both HDFC and HDFC Bank will continue to operate independently till the effective date so that the mortgage business carries on without any disruption.

Let me now quickly explain the structure of the transaction. The transaction involves the amalgamation of HDFC and its two wholly owned subsidiaries, HDFC Holdings and HDFC Investments with HDFC Bank. HDFC Ltd., as you know, is the promoter of HDFC Bank and together with its two subsidiaries currently holds approximately 21% of the share capital of the bank. Post the completion of the merger and subject to regulatory approvals, all the subsidiaries and associate companies of HDFC Ltd. will be owned by HDFC Bank. Based on valuation by the valuers and the fairness opinion, the share exchange ratio has been determined at 42 equity shares of HDFC Bank of face value of Rs. 1 per share for every 25 equity shares of HDFC Ltd. of face value of Rs. 2 per share. The conclusion of this transaction is subject to regulatory and statutory approvals. Post the effective date, HDFC's shareholding of 21% in HDFC Bank will be canceled and this will open up a potential legroom of up to 7% of further holding for FPI's in HDFC Bank. The Bank has requested RBI for phased compliance in terms of timelines for CRR, SLR and priority sector lending requirements. The Bank has also requested RBI to permit the Bank to hold equity in the subsidiaries and associate companies of HDFC Ltd. These requests are under consideration by RBI in terms of the letter dated April 1. The merger will benefit the shareholders of both HDFC and HDFC Bank as follows:

Lower cost of funds will be made available for the mortgage business. The Bank will have access to the time-tested mortgage origination and loan servicing processes of HDFC. The mortgage business has immense potential and hence the merger will help the group enhance its market share consequent to further leveraging on the distribution network of HDFC Bank. The merger will mitigate single product risk while at the same time enhance the diversity of assets for the combined entity. Under the bank's structure. the features of the mortgage product can be enhanced in terms of product design, in line with different products, which are introduced, which are available in the global market. The combined entity will be in a position to offer the mortgage products seamlessly as against the current arrangement between HDFC and HDFC Bank wherein the bank sorts its mortgages and acquires a predetermined percentage of the loans sourced through the assignment route. HDFC Bank currently has 11% of its assets in mortgages. Post-merger, this percentage would increase to over 30% with a potential to grow even higher. The mortgage product will also increase the asset duration of the Bank's retail book. Infusion of capital in the Bank will no longer be required and consequently the drag on the return on equity on the mortgage business will go away. Subject to RBI, SEBI, IRDA, and all other regulatory approvals, material subsidiaries and associate companies of HDFC Ltd. will continue to be owned by HDFC Bank. This will facilitate more efficient cross-selling of banking and financial service products, including insurance and mutual funds. Also, the value of HDFC will not be depressed by the holding company discount in so far as it relates to the shares of the Bank. The proposed merger of HDFC Ltd. and HDFC Bank will, therefore, lead to significant synergies for the combined entity and will lead to better returns for stakeholders.

The proposed merger will benefit the economy in more ways than one. A larger balance sheet and capital base will allow greater flow of credit in to the economy. It will enable underwriting of larger ticket loans, including infrastructure, which is an urgent need of the country. It will enable the delivery of the home loan offering to a large base of over 68 million customers of HDFC Bank in a seamless manner and, inter alia, improve the pace of credit growth in the economy. HDFC is a significant provider of home loans to lower income group and the middle income group segment under the affordable housing initiatives of the Government of India under the Pradhan Mantri Awas Yojana. Access to housing finance for this category would improve further on account of the low cost funds available with HDFC Bank. A larger balance sheet will also facilitate flow of a larger quantum of credit into priority sector, including agriculture. Subject to regulatory approvals, HDFC will continue to operate on an as is basis till the effective date. It's important to note that jobs of each and every HDFC employee will be protected, and whenever required, rules will be reorganized. It is envisaged that all HDFC branches, offices in India will be retained and mortgages will continue to be offered from these outlets. Over a period of time, these branches would be converted to full-service banking branches. HDFC Sales will be a subsidiary of HDFC Bank and HDFC Sales currently sources nearly 52% of HDFC's mortgages. The customer will be the biggest beneficiary and will have access to all financial products under one roof.

We are confident that the workforce will put in all efforts to make this merger a resounding success. Sashi, you want to say something?

Sashi Jagdishan: Thank you, all. Thank you, Mr. Mistry, for these wonderful opening remarks. I think this is a very historic moment. Obviously, it's still not sunk in, but the proof of the pudding would be how we are able to execute, which is our forte over the next three years, and we are very confident for all the remarks Keki has just mentioned. I think we can now fulfil the housing demands of a lot of our customers on a very seamless and efficient basis. Thank you. We open the call for questions now. Thank you very much.

Moderator: Thank you very much, sir. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Suresh Ganapathy from Macquarie. Please go ahead.

Suresh Ganapathy: Hi. Congrats, Sashi and Keki on this historic development. The first question is on the management structure post the merger. I have a couple of questions, so I just wanted an understanding how exactly it's going to work. Like, you are the CEO and Sashi is the CEO of the Bank. So, just trying to understand this a bit better.

Keki Mistry: So, logically, HDFC is merging into the Bank. The CEO of the Bank will continue to be the CEO of the Bank. Personally speaking for myself, I am now 67.5 years old. This merger will probably take another year-and-a-half, by which time, I will be 69 and the retirement age for people in a Bank is 70. As I also mentioned, Suresh, every single employee of HDFC, including all our senior people will now occupy positions within the Bank.

Suresh Ganapathy: The other question is on the treasury shares, which get created and automatically get cancelled. That's some billions of dollars, the way it worked in ICICI Bank and Ltd. was that it got created and then ICICI used to keep selling those shares and book those gains in the P&L. Is that the kind of structure, which will happen in this case or how exactly the monetization will happen here?

Sashi Jagdishan: Suresh, I agree that was the case in that time in that merger. Now, it is not permitted. So, the treasury stock will be cancelled. There won't be promoter holding. It will get canceled against the equity shares of the Bank.

Keki Mistry: Also, Suresh, I think it is important to understand that the entire 21% held by HDFC and HDFC Bank is construed as foreign shareholding. So, when these shares get cancelled, automatically the foreign ownership limit in the Bank has the potential to increase, and I think the increase can be about 7-8%.

Suresh Ganapathy: So, the outstanding number will be 65% foreign holding in the Bank, the combined entity?

Sashi Jagdishan: Around 65-67%.

Suresh Ganapathy: Post merger, the combined entity will have a foreign holding of 65-67%?

Sashi Jagdishan: Of course, we'll have to check out what happens after the regulatory approvals come through.

Suresh Ganapathy: Final question is on the statutory appropriation because the problem and the relaxation that you have sought because what's happened, Keki and Sashi, here is that clearly in one of the recent deals, without taking name, the regulator was not happy with the bank owning more than 10% stake in the insurance company. Now, how confident you are that the RBI will be happy with this kind of a structure because, clearly, they want to ring-fence and go towards a holding company structure that's point number one and the second thing on statutory appropriation, as per my calculations, we'll have to raise Rs. 70,000 crores from the market to meet the CRR and SLR norms just to meet the 22% requirement, 18% SLR and 4% even after factoring in 12.5% on your deposit. So, how do you plan to do all these things.

Sashi Jagdishan: So, a couple of things, Suresh. Number one is, if you look at both our balance sheets, we have been carrying a lot of liquidity, high quality liquid assets, which have been much in excess of our regulatory requirements, and we would continue to do so because that's the liquidity cushion that we have always patronized as a part of our asset liability management, number 1. Number 2 is, as you know, we have been ramping up our distribution over the last couple of years and more so even during the COVID year, we opened over 750 odd branches or 730 odd branches. We still have a large appetite to grow our distribution over the next couple of years. It may be at a faster pace than what we have done this year. So, combination of the fact that both the entities have been building up or having high quality liquid assets much in excess of the regulatory requirements, the fact that we have a large number of distribution expansion plans over the next three years, the fact that a large portion of our existing branch distribution will migrate from a low vantage to a medium to high vantage, which is when you will start to see the multiples of deposit mobilization going in a geometric progression. I think it's all about execution. I think the combined entity will have the where with all to meet the demands of this enhanced regulatory requirements arising out of SLR or CRR or for that matter, priority sector.

Keki Mistry: So, Suresh, to answer your question on the subsidiaries, my sense is there are already banks, which own equity in insurance companies and these are not capped, as you said, at 10%. So, we will, of course, be having detailed discussions with RBI. At the moment, we have sought that the existing subsidiaries of HDFC and our associate companies will continue to be the subsidiaries and associate companies of the Bank.

Sashi Jagdishan: I just realized that I think last evening the team released the quarter results on the exchange, and if you really look at the moment on the deposit mobilization, it's at an all-time high where in the absolute amount of deposit mobilization has been upwards of Rs. 1 lakh crores. So, the organization has that capability. I think when the merger does happen, the fact that we will also get additional branches, which will be converted, as Keki was mentioning, to full-fledged Bank branches, the ability to mobilize more is something that is possible. So, we believe that the regulatory cost, arising out of this, especially on the reserve requirements is much lesser than what it would have been on a previous date.

Suresh Ganapathy: I'll squeeze in one last final question before I sign off. What will be the role of Mr. Deepak Parekh in the combined entity?

Keki Mistry: I think these are all issues, which will get discussed over a period of time, and we are having a press conference at 11:30, so some of these issues will get addressed then.

Suresh Ganapathy: Thanks so much, Keki and Sashi. All the best.

Moderator: Thank you. The next question is from the line of Mahrukh Adajania from Edelweiss. Please go ahead.

Mahrukh Adajania: Congratulations to HDFC and HDFC Bank. My question is similar to Suresh's. Are you very confident that RBI will not insist on the NOFHC structure for the subsidiaries?

Sashi Jagdishan: Mahrukh, thank you for the question. As of now, we have kept the proposed amalgamation rather elegantly, but in the event that there is a need, we are happy to even go ahead with any structure or an alternate structure that the regulator may want us to do.

Keki Mistry: But Mahrukh immediately the plan is to continue that HDFC Bank will be an operating bank as well as holder in equity of other businesses like insurance, asset management and so on and so forth, and there is existing precedence to that effect. If and when in future, RBI requires these banks to move to a holding company model, then at that stage, the bank will of course look at it and do it.

Mahrukh Adajania: Makes sense. My other question was on the priority sector that you mentioned, you of course mentioned on PSLCs, etc., so the priority requirement of the merged entity or the merged bank, will that be lower than the current?

Sashi Jagdishan: No, Mahrukh, the fact that the merged entity will assume the loans of HDFC Ltd., which is at this juncture about Rs. 5,23,000 crores and probably it will be higher at the time when the regulatory approvals come over. The impact on what is required in terms of priority sector requirement will be much higher at that point in time. What Keki mentioned was that today we have an avenue or multiple avenues to meet that kind of a requirement. Yes, PSLC allows us the flexibility of meeting those requirements without the need for any incremental funding. So, of course, today if you look at the market, there is almost about Rs. 5,50,000 crores of PSLC's being traded on an annual basis and I'm sure, as the banks grow, this particular market will only increase. In the initial period, we will probably seek higher proportion of our requirements through the PSLC route. Having said that, if you have seen our recent forays into the rural and semi-urban markets, we have been stepping up our MSME businesses over the last year or so. That has been growing pretty strongly. Even in this quarter, I believe, we grew at about 30% year-on-year or a sequential growth of 8%. So, we have a fair amount of strategies to execute in terms of meeting this enhanced requirement from priority sector. So, combination of what we can do organically, what we can do through the PSLCs is what our thought process is. Yes, it's not easy. It's going to be at a larger scale, but I guess the combined might of this institution once this happens and this transaction get consummated, the fact that we are not today offering mortgages especially in the semi-urban and rural branches of the country, we can start to do that. That will be an additional benefit arising on the PSL portfolio. So, these are some of the thoughts, but it's a lot of hard work, but the entity is well geared to take on this challenge.

Mahrukh Adajania: Sure. Thanks. I just have two more questions. The first one is that you did mention about HDFC DSA, so that will become the subsidiary of the bank now, right? Will they be only doing home loans or they can do other loans as well now?

Keki Mistry: Correct and that is something, which will progress over the coming years. We will figure that out, but I guess they can also then start looking at distributing a much wider range of products for the bank.

Mahrukh Adajania: Got it. And my last question is a clarification. You said what percentage of HDFC Bank customers don't own mortgages?

Sashi Jagdishan: Okay, we have 68 million customers today and its growing at a clip, on an annualized basis, of about 10 million customers. Annualized, the run rate is about 10 million. The reality is that the penetration of mortgages in our book currently is very low. As Keki mentioned, once you open up the distribution, where we are able to offer mortgages across all our branches across all our virtual channels, across our digital platforms and the friction that is there today in the processes of lead origination and sanctions and disbursals will come down significantly that will help us to be very competitive in the markets for distributing the home loans product once this transaction comes through. We believe that the moment you start to penetrate more into your base, which is very similar to what we have done in any other retail asset product, if you look at it, we are reasonably a strong market player in retail assets ex mortgages, so this is something that is lacking in us in this particular distribution of ours. I think once this product comes on to the board easily to all the branches and our other platforms, the penetration levels moving up itself will power the whole engine of the Bank.

Mahrukh Adajania: Thanks a lot.

Moderator: Thank you. The next question is from Adarsh Parasrampuria from CLSA. Please go ahead.

Adarsh Parasrampuria: Hi, and big congrats to both the teams. I had one question. When would you call the merger a resounding success? What would be the metrics you would use to judge that? I just thought there will be initial cost to the P&L for the transition, but there's still a big gap between cost of funds of Limited versus the Bank, would that be the direction over the course of the next two years where you get a lot of benefits to say that would be a metric that would be used to judge?

Keki Mistry: So what will happen, Adarsh, is that as HDFC branches start mobilizing other products and savings and current account deposits, the overall funding cost of the bank would come down. Present HDFC structure does not permit us, as you know, to accept current account and savings account money and effectively what will happen is because of the merger, the overall cost of funds will come down. As the overall cost of funds will come down, to my mind, it will offset any additional cost that is entailed in terms of CRR, SLR, priority sector or anything else.

Sashi Jagdishan: And just to add to what Keki is saying, this is a very sticky product, and the lifetime value of a customer's relationship with that Bank just enhances when you start to put a mortgage into his product offering. One of the metrics that we would like to watch is what is what are the penetration levels of mortgage to our customer base. The moment that starts to move from a low percentage that is there currently even to higher levels, that itself will demonstrate the ways our balance sheet will start to move. As I mentioned in the earlier conversation, this is going to be powering the moment we start to expand our penetration to our customer base.

Adarsh Parasrampuria: Got it. And Sashi, you did mention that the structure is being done elegantly for holding of subsidiaries, anything that you could share? I understand that you seek regulatory permissions, but is it like just all the percentages stake will be held under the Bank, that would be the current proposed structure, I believe, or is there something more than that?

Keki Mistry: Yes, that is the envisaged structure.

Adarsh Parasrampuria: Perfect, thanks and congrats again, quite a big moment.

Moderator: Thank you. The next question is from Anand Dama from Emkay Global. Please go ahead.

Anand Dama: Thank you for the opportunity. Sir, how will the tech integration happen, and what will be the overall integration cost, any thoughts over that?

Sashi Jagdishan: Fortunately, this is a single product Company, which will be integrated into the technology architecture of the bank, it is not as complicated as a transaction system where you have very high levels of velocity in that particular technology systems. So, this is like any other retail asset system that we would have. So, all that needs to be done is to integrate into our main core system or the GL system, that's the first. But not many people have been socialized on this particular aspect. During the course of now to the effective date, we will examine the scalability, the resiliency, and the robustness of the system of home loans and other surround systems as well, and we will take adequate calls in terms of what is required, whether there is any change required, whether there is a change in the architecture or whether if it is good enough for us to continue with the same. So, these are decisions that we will probably look at it, as we start to engage more and more from now to the effective date.

Anand Dama: Can you put some figure to the integration cost that you will incur?

Sashi Jagdishan: It's too early for us to even estimate that, at this juncture, but considering the fact that we are already expanding our investments, whether it's in distribution, whether it's in technology, whether it's in people, I don't see this to be a very significant proportion of our merger expenditure.

Anand Dama: And you said the affordable housing bonds that you have is about Rs. 70,000 odd crores?

Keki Mistry: It's about Rs. 80,000 crores housing bonds with seven years original maturity.

Anand Dama: So, on that, you don't have to maintain CRR, SLR?

Keki Mistry: That is as per the guidelines of covering this particular regulation from RBI, but obviously everything is ultimately subject to approval from RBI.

Anand Dama: And sir lastly, will you also have to merge the HDB Financial Services because I think one of the rationales that you gave for this merger was that you expect at some point of time the holding company structure norms would come and the lending business will have to switch into the bank. So, does it mean that HDB Financial Services also could be merged?

Sashi Jagdishan: We will await some regulatory clarifications on the same and we will abide by whatever is the regulatory directions on that particular aspect.

Anand Dama: Sure, sir, thanks a lot.

Moderator: Thank you. The next question is from the line of Seshadri Sen from Alchemy Capital. Please go ahead.

Seshadri Sen: Thanks for the opportunity. Congrats Keki and Sashi on a game-changing deal. I have a couple of questions. One is a follow up to Suresh's question on the CRR, SLR, so is it now that the Bank will start to build up on this excess liquidity leading up to say the 1.5 to 2 years that we get on the merger so that at the time of the merger, you are ready to fulfil all the CRR, SLR requirements, so this excess liquidity that is there on your balance sheet will go up from here?

Sashi Jagdishan: I would say yes. We need to have a very planned approach, a phased-in approach so that we really are not caught to mobilize it in the shorter end. The transaction time for this particular regulatory approval, I believe, will be anywhere between 15 and 18 months. So, we have enough time for us to start mobilizing the extra reserves and also in terms of the profits.

Keki Mistry: Also, I would add that the Bank has sought time from RBI to meet these requirements of CRR, SLR, and priority sector, and let's wait for them to come back to us with their final decision.

Seshadri Sen: Understood, thank you. The second question is how will the merged entity approach the developer business? It's something that HDFC Bank has traditionally stayed away. Now, you are inheriting a developer business. Will you continue to grow it as long as it stays within the RBI designated limit or is it something that you will choose over a period of time to runoff?

Keki Mistry: One of the ways, Seshadri, to garner individual retail business is to also give construction finance loans to property developers. So, the Bank would probably continue to give developer loans, but let Sashi answer that.

Sashi Jagdishan: The very fact that this is going to be a lift and shift in terms of dovetailing into the Bank, obviously you are right, we don't have that expertise currently, but as Keki mentioned, the entire human capital will all seamlessly integrate with that of the Bank, so will the expertise on the construction finance, even that will also get embedded in the Bank as well. So, we will ride on that expertise and then later on I am sure that expertise will be socialized to a larger proportion of our credit verticals as well. So, this is our thought process, and as Keki mentioned, since this is extremely important for the mortgage business, we will have to do this, but having said that, we are very clear that once this becomes the Bank, this will be compliant with all the regulations that is expected out of a Bank even on the construction finance.

Seshadri Sen: Understood, thanks. In fact, to slip in a third, jumping the gun here a little bit, but the Bank is now a little bit of open architecture on insurance distribution, once the insurance company becomes a subsidiary, is that a situation that you can or thinking of revisiting?

Sashi Jagdishan: Not really. The rationale for open architecture is to offer the choice and options to our customer base. That philosophy continues to be there and will be there. So, we will continue to patronize open architecture even post merger.

Seshadri Sen: Thank you, and congrats again for a great shareholder friendly decision.

Moderator: Thank you. The next question is from the line of Nitin Agarwal from Motilal Oswal. Please go ahead.

Nitin Agarwal: Congratulations on the merger. It's a really big historic moment. I want to understand on the OPEX part. This quarter we have added, as a Bank, over 560 branches and now as we look to absorb all the employees of HDFC Ltd. and also gain from the branch network of HDFC Ltd., so will that mean that we will like to go slow in terms of our own branch expansion, and how will that change our medium term cost ratios outlook, which we have earlier indicated at times to reach 35% cost-income?

Sashi Jagdishan: Dear Nitin, we have a strong appetite to continue to invest in distribution, continue to invest in technology, continue to invest in human capital. With this product advantage that the Bank will now get, we probably will be setting up our distribution even more. So, our investments will be even more. We will be happy to make these investments. I am happy even if the cost to income for a while even deteriorates, but definitely we are very sure that once the investments have plateaued, the operating efficiencies will kick in and the glide path that we had given that from the time of the peak of the investments to and when you start to get the efficiencies on the operating leverage kick in, we will start to see the cost to earnings come down even further from that level. So, on a merged entity today I think we are 36-37%, as Keki mentioned it's just about 8%, so on a merged basis, it could be somewhere around the 32-33% or in that range, happy to take it even further just to ensure that we are not cringing on investments, even if that were to go, but we are sure in the medium to long term, we will see a glide path of the operating cost to earnings coming down.

Nitin Agarwal: Sure, sir, thanks so much.

Moderator: Thank you. The next question is from Jai Mundhra from B&K Securities. Please go ahead.

Jai Mundhra: Congratulations, and thanks for the opportunity. I wanted to check if you have calculated and broadly by which year, the measure could be EPS accretive because clearly proforma number as shown in the slide, there is a 3% accretion, but of course there would be some drag on CRR/SLR/PSL front, so just wanted to check your thoughts on by when the mergers should be EPS accretive?

Keki Mistry: Well, to my mind, the merger will be EPS accretive from the first year itself because 21% of the shares automatically get cancelled.

Jai Mundhra: And any ballpark number on CET-1 impact of the merged entity apart from the investment, which is there in the HDFC Ltd, which will be extinguished?

Keki Mistry : So, it will be a positive impact because HDFC's tier 1 capital currently stands at over 22% and this 22% is also calculated after reducing the investment made by HDFC in the bank. So, when that gets cancelled, the capital will go up and therefore overall from a capital adequacy perspective, it will be higher.

Jai Mundhra: Sure, and the last thing sir, you have mentioned that in the meanwhile in the run-up to the transaction, there would be some adjustment to the banking model, so just wanted to check what it could be, would it be in terms of Limited sourcing more PSL assets or let us say moving to external benchmark sort of a regime or what all could it entail?

Keki Mistry: No, nothing, everything remains the same till the effective date and upon the effective date, the branches of HDFC will then, over a period of time, start becoming full-fledged branches of the bank, otherwise nothing else changes. It's business as usual.

Jai Mundhra: Right, it's just that it says that there would be some opportunity to normalize for adjustment to the banking model, so I was thinking if there is something…

Keki Mistry : No, there is nothing significant difference in terms of regulations between NBFC and the Bank. Whatever little differences might be there, we will of course do things going forward, which will be compliant with the banking model, but that does not have any material impact on our balance sheet or our profit and loss account.

Jai Mundhra: Sure, thank you, sir.

Moderator: Thank you. Ladies and Gentleman, that was the last question. I now hand the conference over to Mr. Keki Mistry and Mr. Sashi Jagdishan for closing comments.

Keki Mistry: I just wanted to say at the end that to our minds this is very accretive from the perspective of shareholders of both HDFC and HDFC Bank. We will now be able to leverage the lower cost of funds of the Bank together with its huge distribution platform and its huge distribution reach with the efficiency in the mortgage product, which HDFC has developed over the last 40+ years, and also the fact that cost-income ratio currently stands at 8.1%. So, I think in terms of combination to my mind, this is probably one of the best combinations we could have had. Earlier, this did not make as accretive a sense as it does today because of some of the reasons that I mentioned in the beginning, higher CRR, SLR requirement, priority sector, you actually had to go and borrow money, and so on so forth, but today it's, as we believe, EPS accretive from year one. Thank you very much.

Sashi Jagdishan: Thank you everyone.

Moderator: Thank you. Ladies and gentleman, with that we conclude this conference call. We thank you all for joining us.