IDFC FIRST Bank
ALWAYS YOU FIRST

We don’t want to be in infrastructure, just want to be a fantastic consumer bank: V Vaidyanathan, IDFC FIRST Bank

Synopsis:

IDFC FIRST has brought down the bank’s infrastructure book down to Rs 11,000 crore from Rs 22,000 crore at the time of the merger and plans to bring it down to almost nil over the next two or three years.

By ET Now

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__V Vaidyanathan__, Managing Director & Chief Executive Officer, __IDFC FIRST Bank,__ says __Morgan Stanley__ has always talked about the bank’s low __ROE__ but he is confident that it will touch 18% soon.

The Budget has surprised us, growth is back from the throes of pandemic and things are indeed looking up. What’s your view?
No doubt about it! All indicators that are coming across all sectors, be it FMCG or sales of tractors and vehicles, everything is looking up now.

Things are looking up for IDFC FIRST Bank as well, but there is a historical challenge in the MSE and SME books. While the retail book is growing, how to address the other aspect?
There is no challenge in the MSE and SME book. The challenge was in the large corporate and infrastructure exposures. Our infrastructure exposure at the time of the merger was Rs 22,000 crore. We are very aware that infrastructure has to come down because it has its own challenges. We have brought down the **infrastructure book** down to Rs 11,000 crore. Our game plan is to bring it down to almost nil over the next two or three years. **MSME** and consumer are our staple business and that is doing fantastically well.

I want to understand the CASA side of your business. You are offering the best rates and the industry has helped you to get a lot of low-cost deposits. What happens next? Obviously, you cannot pay such high rates for savings?
Two things. First off all, we had a historical borrowing rate because IDFC Ltd. was a DFI and had borrowed at about 8.5% and even Capital First and **NBFC** had borrowed around that rate. So, we had a large borrowing at that rate. So, we keep it at 7%, which is a good rate compared to 8.5% and we kept swapping that money. But that was then.

The important thing is that our incremental flow from the customers on CASA has been phenomenal and our CASA rate has now touched 48% and we are feeling very comfortable. The liquidity in the bank is Rs 17,000 crore. Obviously, we do not need to pay 7% anymore and we have brought down rates to 6%. But frankly, we are a very customer-first organisation and even at 6%, we have one of most attractive rates in the market today. Change to 6% will also increase the net interest margins.

The Morgan Stanley report dated 31st of December is calling you one of the most expensive banks looking at the underlying growth. Your take?
They have always called us the most expensive, overvalued bank. In this report, they made a mistake which I think is an honest one. I do not think there is malice behind it, but they made a mistake whereby they added the bonds exposure and non-funded exposure on the numerator but the denominator they forgot to add. So, the net of its numbers are much lesser than what they have represented. It is a general mistake and they openly fixed that.

But stepping away from that, they have always been wrong about us. Let me just say one more thing, they are just being very mathematical about us. But how do you value a phenomenal intellectual property the bank is building? How do you value the fact that this bank is showing the capability of growing from Rs 100 crore to Rs 30,000 crore, from Rs 30,000 crore to Rs 60,000 crore and now we are projected to be Rs 1 lakh crore? They have not given any valuation for that kind of growth on the retail side. They cannot see the fact that NIM has grown by 1.5%-1.6% to 4.6%; they cannot see PPOP has moved from Rs 30 crore pre-merger to Rs 500 crore even without treasury. They are just going on and on, on one issue -- that ROE is low.

Fine our ROE will come, it will come because we are building a good bank. It will be in mid-teens and it will be a 18% ROE in my opinion.

When do you think ROA and ROE will be around industry averages?
Definitely we are getting there. Let us just get back to the core. The core is the ability to lend in a safe, risk-adjusted manner and we have demonstrated that capability quite a number of times, In Capital First, the NIM was 9%; in this bank our NIM has already touched 4.6%. On the retail side, now we are able to borrow money at 6% incrementally because the saving rates are 6% at the peak. We are going to borrow money at 6%, our lending is on an average at around 15% but we lend anywhere between 9% and 20% odd depending on the product segment. If we borrow at 6% and lend at 15%, we have to make money, it has to become ROE accretive.

Overtime, infrastructure problems will go away, overtime some of the corporate loan issues will all go away. It is a matter of time, they have already started going away. By the way, our credit loss is only 2% because our credit quality is improving. So, if you lend at 15-16% and you have a 2% credit loss, there is a 14% risk adjusted money. You are borrowing money at 6%. It is pretty plain that the bank has to make money and it has to be ROE positive. So, my sense is that ROE will come, it is only a matter of time.

Is it a right way to look at a bank purely based on price to book or should one look at PE multiples because ultimately it is about growth? In your case, I can slice your book in many ways depending on my assumption rather than focusing on absolute growth?

Well, banks raise equity from time to time and hence the price to book becomes a benchmark but even in terms of price to book, people normally factor return on equity in the equation and that is one of the reasons Morgan Stanley goes after us every time saying our ROE is low.

But anyway, coming back to the ROE point, they are looking at us at a 2% ROE today but they should not forget that in our previous company, we moved the ROE from negative to 15%, in fact, heading towards 20%. So even here, ROE will come. I have explained to you the reason why price to book is used as a benchmark.

By the way consumer companies are valued at price to earnings. We are not a consumer company. We are 60% retail and in the next two, three years, we will probably be 80% retail and can be considered a consumer company.

Ultimately banks are a play on economy and consumers. Why should we look at historical benchmarks? But we will keep that conversation for some other time...

No, it is also because of the corporate loans. If you take a consumer company and think of it like a consumer company, you can value it like a consumer company.

The government is committed to spend a lot on the infrastructure sector. Once the bad bank and other factors come into play, things would dramatically change there. Could the legacy problem be a future growth driver? Are we looking at that kind of a scenario?

No, no, we are not going there at all. First of all, what the government has done on infrastructure is fantastic and as an Indian, as a resident of this country, we obviously feel proud that someone is going after infrastructure the way this government is doing. It is not just the bad bank and not just that Rs 20,000 crore and DFI, it is also the kind of investment that the government is putting out in infrastructure.

The amount seems crazy but we will have a derived advantage of all that investment. Derived advantage meaning when money goes into roads, ports, infrastructure etc., it goes to the vendors; vendors have contractors, contractors have employees and there's a whole chain. Once cement and steel and everything starts moving, consumption moves. We will have a derived play of consumption. Infrastructure has its own challenges and everybody recognises that. We are not going there, short answer. We just want to be a fantastic consumer bank, a well growing, good risk management, good corporate governance, consumer bank.

In today's world, everything is going digital and fintech disruptions are happening in the consumer banking and the consumer retail space, how will you differentiate yourself?

We are really at the forefront of that. We love it first of all because we know that game. We had played that game for 10 years. Basically, these games can be very unnerving for those who do not know the game. But that is where we were born. We were born a fintech. For example, we have the ability to give out consumer loans after doing all kinds of algorithms of fraud, analytics, credit view, everything in a matter of seconds. We know we give out three to four million loans per year through the use of technology.

Even on the liability side we use technology to create effect. The kind of CASA we have got is also because of our technology capability and not just because of pricing. The short answer is that we are very good in that space and we will lead on the front. There are new apps coming up which are very advanced, you can have a look at that.

A very basic yardstick which markets, and investors use is what is the promoter's commitment to its business, that is ownership patterns. Your ownership has been gliding down. Has that been done consciously and if you have sold, why?
Actually it had a sequence. I know what you are referring to. When it was Capital First, I gave away stock to some people because I thought they all helped with the company and it was about 20 odd percent of my holding. When Corona happened, I had to sell a significant holding because I am not a generational wealthy guy. I borrowed money to buy the stock and did leverage to buy out of the prior company. So, I had leverage and in Corona, I got stuck. So, I sold. Then later I gifted some stock to some people whom I thought were very valuable in my life in the past. Wealth is good only when it rotates and when it keeps moving on rather than getting accumulated to one demat account. It has got nothing to do with commitment. My commitment is 100%. The bank is 100% mine. I work like that. So, no investor needs to worry about that.

Is there leverage which you took when you committed to this transaction? Is that leverage still there on your balance sheet or is it over?
It is over. I had to square it at the depth of corona at Rs 20 rupees or something. But such was the moment. But I do not have any leverage on account of those matters anymore.

On one side, there are some investors who are asking why is Mr. Vaidyanathan reducing stake? The other set of investors especially on social media said Mr. Vaidyanathan is running this bank and this bank is going to be a turnaround one and a big one looking at his past experiences. For the worried investors, you have addressed the concerns, for those who

are excited about what you can do, should you temper it down?
I am very aware that a lot of people believe that they should put all the money in this bank because it has a good future. My honest answer would be that you should diversify. No matter how much you trust a bank on the equity front, equity has its own ups and downs. There may be other banks who are ahead of the curve than us, who started may be 20 years before us or 15 years and are ahead of the curve in ROA and ROE. But we are catching up.

In the long run, we will be a fantastic bank, but you should diversify. But on the deposit side, you can be 100% assured, this is a fantastic bank. Your money is like 1000% safe. Just sleep well.

So the saving rates which you are offering, where do you think that will settle?
First of all, when we started paying 7%, we were paying it across pockets; then we paid 7% only up to Rs 10 crore; then we paid 7% only on savings up to Rs 1 crore. Now we are paying 6% only and that is the peak rate. Basically, the strength of the bank, the liquidity is strong and so we reduced it.

Going forward, if you ask whether we are going to reduce it further, my view is not in the near future. Near future means the next five or six months. Beyond that, who knows?

The big picture is that in the banking sector, consolidation is evident. How do you see the landscape of the Indian banking sector changing? Will the number of banks become less and will the relevance of small banks be completely gone?
Not at all. Small and medium banks are catering to specific needs and therefore everyone has a space. No one bank, not State Bank of India, not any of the big four, can meet all the needs of this country. Everybody has

their own criteria and like we say product programmes of respective banks by themselves are not inclusive. They are exclusive. There will be space for lots of small finance banks. In fact, I would personally wish that India comes out with a lot more small finance banks which can cater to these needs. India also needs a lot of more universal banks. In fact, consolidation of banks is not a good solution. Privatisation is a good idea.

For any consumer bank like yours, where there is a very large fee-based component. But in today's zero broking environment where fintech has disrupted everything, would fee-based income spreads come under pressure?
It depends on how you look at it because if your book is growing and the businesses operations are increasing, fee-based income can keep increasing. But we are very clear that we do not want to see any fee-based income which is made at the cost of trying to pinch the customer's pocket in an incorrect sort of way.

But generally speaking, I feel that fee income will continue to grow because you offer more service and collect your fee. We are also launching credit cards and that again is a line of business for us.

Yes, that is a disruptive launch. Isn't it? The kind of fee you are charging has set the cat among the pigeons!
Well the intention was not to set any cat among any pigeons, but I always think of expanding markets. In India, for 30 years, interest rates have been 38-40% on credit cards. Cash withdrawal is even more expensive. So, we just thought that we could price customers individually, based on certain algorithms and logics and even on cash advance, the fee structure in India has been very high. I think customers are beginning to like it.