IDFC FIRST Bank
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Mr. V Vaidyanathan, MD & CEO – IDFC FIRST Bank speaks to ET Now on Q1 FY22 results

Anchor: Nikunj Dalmia, Managing Editor, ET Now

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Nikunj: Okay it gives me great pleasure now to bring on board Mr. V Vaidyanathan, Managing Director & CEO, IDFC FIRST Bank to walk us through, what transpired in the quarter gone by and what should you expect by 2022, what is the understanding of the Covid provisioning and focus. Thank you Mr. Vaidyanathan. Good morning and thank you for joining us. Let's spend some time on why the headline numbers don't look impressive and what is the inside story? Why is there is a significant drop in the profits and an uptick in NPAs?

Mr. Vaidyanathan: Actually, it's very simple. This is the question everyone is asking. Thank you for asking the question straight forward. Now you know last quarter, for two out of 3 months, basically there were lockdowns. The nature of our business is that customers who do not pay in a particular bucket they tend to move to the next stage of delinquency so that's what played out, we have a provisioning formula, and our formula recognizes losses very early so our first quarter provision numbers came rather high. Our understanding is, based on how we know our formula, our second quarter provisions will be much lesser than third quarter and fourth quarter provision will be even less than the third quarter. If you see the story in the last two and a half years, the core operating profit up is going one way up, already it has touched the highest ever core pre provisioning profits at Rs. 601 crore. So, if that number of Rs. 600 crore moves up and provision comes down, which is what we are expecting, profit will automatically go up over the next three quarters.

Nikunj: Okay, when you looked at the Covid provisioning, do you think you have been very aggressive in the entire Covid provisioning last quarter or the current quarter - I am just trying to understand the whole approach?

Mr. V Vaidyanathan: Yes, see the approach is that we have a formula very stage-wise. We have a formula and we follow it. The key thing is, we had an exposure to Dewan Housing, Reliance Capital, we had large exposures, large exposure in infrastructure, but when we lost the money, we lost it for good, we never recovered anything more, meaning we got only 25 cents to a dollar. But in retail, just because we have taken a provision, doesn't mean customers need not pay, customers still owes us the money. So, when the economy revives, customers tend to pay back. Our experience is that even after provisions, quarter-on-quarter for years to come, money tends to come back. So, yes it has been rather early-stage recognition so to say but we think money will come back.

Nikunj: What would you say has happened to the recovery in the first two months of this quarter because what we are discussing essentially are numbers till June, now we are in August so for the first, not two months but for the first one month of this quarter.

Mr. V Vaidyanathan: No, actually, not just the one month, but from the 15th of June to the end of June we have that data point, so let me share July numbers, one of the key things we have noted is that as follows: when wave one ended, somewhere in September 20 or so, every month after that recovery kept going up and by March 2021 our recovery crossed 100 percent of pre-Covid, as if Covid never happened, that is March 2020. Now after wave 2 ended in June, lockdown ended, in July our collections have crossed pre-Covid numbers. So, when we say our provisions will come down quarter on quarter, it is not just hope, it is based on these numbers– our straight answer is – our collection is 99.5 percent of the earliest bucket, in our internal terms we call it X bucket, the early bucket, so that has crossed 99.5 percent and we are feeling good about that. So, it provisions is on its way down and you will see in the next three quarters, so basically investors should not get worried about this. This is on record on your show today and you can keep this on record.

Nikunj: Okay, so what happens to your credit cost given that the last quarter have changed everything?

Mr. Vaidyanathan: Yes, our credit cost, see last quarter we have taken a provision of Rs. 1800 crore. Now our credit cost guidance for this year is that if ballpark about Rs. 3000 crore on an average loan book of about Rs. 1,23,000 crore, so Rs. 3000 on Rs. 1,23,000 works out to 2.5%. Our belief is frankly for a business like ours, with yields of upwards of 14% to have a 2.5% credit loss – that too in a Covid year when lockdown impact is upon us, and wave 2 effect is still there, to get 2.5% - I think it talks really well about our portfolio. In fact, our guidance again is that for the next year as the portfolio matures, we see a 2% is our guidance for credit cost - on a sustainable basis.

Nikunj: Okay, when a bank goes through a complete change because of an external factor - Covid is an external factor - how do you deal with it?

Mr. Vaidyanathan: See I have seen much in my life, for say about 25 years in this industry, some problems come and go, in 2016 there was demonetization, demonetization felt like everything was collapsing around. In 2017 there was GST, you know, then there is Covid now in so many cycles - we should not alter our longer term picture on the basis of what is coming out, we must strengthen, learn and keep moving on. My short answer to that is that we will continue to stay focused on the big story. We believe that from a loan book of Rs. 94 crore to Rs. 30,000 crore to merger, now it is Rs. 75000 crore – with the Indian upcoming story– it could be Rs. 2 lakh crore or Rs. 5 lakh crore or Rs. 10 lac crores – it can grow to anything in our lifetime but as long as we are stable in our strategy, I think it’s a mega bank coming up as far as our bank is concerned and it can’t be stopped.

Nikunj: Okay, you know I am getting very different sound vibes of where the retail book is headed and looking at your peers / companies or banks which have declared their

numbers. Why we are not getting any clear messaging from let's say on the retail book – is there confusion / is there because different clients various bank has.

Mr. Vaidyanathan: You see, the NPAs - most banks who have reported in the Indian market - everybody on the retail side has reported higher credit losses, higher NPAs, everything, so typically you find that people have reported between 4% and 7% Gross NPA / Net NPA depending on the provision policies. My sense is that you know when you are in the mid of wave, you tend to be a little muddled about where this will go. But I have seen enough to see that on a stable side basis, you know auto loan business is about 0.5% credit loss, if you do a credit card is probably 3 or 4% credit loss, if you do two wheeler business it's 3%, if you do consumable durables business its 5%, if you do a personal loan its 2% and you do home loan business practically it's no loss business may be .1 percent so, if you see--- think that may roughly hold. Honestly, I don't think there is an underlying issue at all. It's just an over cycle.

Nikunj: So let me address three important verticals for your bank one is CV, second is SME and third is MFI. Again I am looking at the number which is from Bandhan and Ujjivan and their comments you got from them what is happening to the auto portfolio various other banks and what Mahindra and Mahindra Financials have reported looks like there is stress in the vertical, what happens now, what happens to you because you have presence in the SME space and the micro finance space and in the auto space.

Mr. Vaidyanathan: Okay, I will tell you the numbers if that helps you. We have three business we do in the vehicle financing, and frankly the vehicle business got affected more. It has run very well for 8 to 10 years. Covid comes when it comes we have to deal with it. We are in commercial vehicles and as Covid struck, trucks stopped plying and they were losing money. When it plies again, they will pay you back, I start from that philosophy. So coming back to the point commercial vehicle does get effected. Our two wheeler financing portfolio. We are dealing with customer base which is relatively a lower income profile by definition. That is why they are buying two wheelers, otherwise they would have bought cars. The income profile are little weaker. When the crises come, economy is in trouble, commercial vehicles is a livelihood financing business, customers they get affected. But really we should see, we should not change the strategy. We have 6, 700 crores JLG business. Are we affected? The answer is yes. Does it mean we lose confidence in the JLG business ? The answer is no. It's like in two wheeler business we have done fantastic property. We've been in business for ten years. We earn 20% we lose 3%, and we are quite proud of it for that. So we just need to change according to the situation.

Nikunj: What happens to the schemes which you had launched, and they were a unique scheme. You came up with a credit card scheme where the first credit card where even if you are late on your credit card payments, interest rates were significantly lower. Your savings rate were very high and that was aimed to largely to CASA.

Mr. Vaidyanathan: The fact is that, I always think about it like this, look we got one opportunity in our lifetime to build a great bank. So, I believe that these are rare opportunities that we get. Now, in this one opportunity in the lifetime, just to build a really great bank where every one of our products should talk about our ethos. It's not for nothing that internally we tell our employees this. We have made a new stamp these days. It's called Ethical, Transparent banking. We make a seal out if it and give it to our employees. There's a reason. So, we say every product we make, we say should be something different something special for the customer. I will give an example. Credit cards. Every time forever since 30 years, APR is the country is 40%. Now we are saying, we are a new bank and we have started 9% to 36%. Everyone wins with our bank. Fees, everybody bills customers fees. We are not saying that's a wrong thing, it is their model. But, we are telling customers before they go to their over the limit, hey listen, you already touched 80%, don't go over limit, otherwise we have to bill you. So, these are genuinely high-quality approach brought to the sector. Even on savings accounts, since independence till today almost every bank pays savings account on quarterly basis, but they take EMI on a monthly basis. We started this model of saying that we will pay interest on a monthly basis. So, I think we are very fetished about this idea of being of making something special.

Nikunj: You know markets got excited when the new RBI rules for the definition came when it comes to the holding company and merger of banks with holding companies. How should one understand the way forward for IDFC Bank and IDFC Merger?

Mr. Vaidyanathan: The truth is that we haven't yet talked between the two institutions on how to go about this because I think actually norms have not come. They have just permitted some small finance banks to apply. So, we will wait for the guidelines and ensure the corporate bank's board will talk about that.

Nikunj: Twenty-four months if the merger goes through, what changes for the shareholders and if the merger does not goes through, what changes for your shareholders?

Mr. Vaidyanathan: You are running ahead. I can't really comment on that at all.

Nikunj: I am trying to build a scenario. Let's say for a shareholder of IDFC Bank Ltd and for an shareholder of IDFC. There are two scenarios which we work with. One the merger happens, second the merger does not happens. So, what happens in both the scenario. Mean, independently, if both the franchise have to remain separate. Then what happens.

Mr. Vaidyanathan: No, I really can't comment. All, what I can say lets talk about it when the guidelines come out and all that. But, I can say that our Bank is on a pretty steady path and we are very proud about building the Bank and we are very proud about our unit economics. Our borrowing rate is less than 5%. Our lending rate on retail is 14%. We can incrementally lend at 9.5%. So, that is the fantastic model we can keep going. Now, these shareholder issues we will deal with, but at this point of time we are more interested in building a great bank and I think that story is rock steady.

Nikunj: What is the preparedness gone forward if there is a third wave?

Mr. Vaidyanathan: See, when the wave one came, it took most people took as a black swan event and actually the fact that the lockdown that happened that was a real black swan event and it was not really the Covid. Now, what we did at that point of time is that we quickly readjusted our credit criteria to adjust for Covid affected industry, touch-based industry, like hotels, restaurants, all kind of related financing. Now, once we did that adjustment after Covid wave one, we have got something very interesting and you should take note of this really that we have in last 12 months post Covid wave 1, we disbursed something like 30-35,000 odd crores and when Covid wave 2 came and the lockdown happened, the collections on the booking between this period did not get affected with Covid second wave. So, the short answer is that we made changes to our model, ie, credit criteria and adjusted it for Covid sort of lockdown effect of touch-based industry and we should be ok. I think that you should expect and frankly if you have noticed the impact of wave 2 was lesser than wave 1 and the impact of wave 3, if at all, will be hopefully, even lesser than wave 2. So, we will deal with it. I think our guidance of 2% credit loss for the next year on the average book is that's what I will hold to.

Nikunj: And you feel that would stay even if going forward there is a third wave. I am just putting that caveat into place.

Mr. Vaidyanathan Yes, of course. Covid wave 3, God knows, if it comes and how big it will be and how much is the lockdown etc., we will have to play to the occasion. I really can't speculate, but I can say that if it's a benign wave, like how wave 2 was or smaller than that, then all our numbers hold. And I can tell you that even for the last year, if you take for 2021, if you take the credit loss that we took to the books, it compares pretty much favorably for similar businesses. This year we are guiding for 2.5%. I would say for the yield we get in this business, any banker will give a right arm and let to get a yield of 14% with loss only 2%. So, even for this year, 2.5%, I think compares very well with the industry and I think for next year guidance of 2% on a stable basis and again I think it's a pretty good number and we feel very confident about that. The only thing is that all these number has not factored one telecom account and that will play as it comes.

Nikunj: How exactly have you positioned for that telecom account in your books? I am saying that as of now we know that there is one telecom company where AGR issues is not sorted. How have you really provided for that account in your balance sheet?

Mr. Vaidyanathan: Right now we have an exposure of Rs 3,200 crore and we have a provision of something like Rs 475 crore or 500 crore. It is about 15% of the total exposure or you can call it 25% of the funded exposure. That's the provision we have. It's better provided than I think most people in the banking system would have provided for that account. The issue is not provision. Issue is that we got to wait for that event to play out and we really believe and hope that the entity stays in place. When we think of it, we have faced enough bullets in life; we have faced Reliance Capital we faced Dewan, we faced infrastructure. This quarter we faced account in Mumbai of 860 crores. We have taken every hit and we can take a hit in the future. Because our incremental unit economics are fantastic. But the bigger issue which I feel is more as a citizen is that it will be a real tragedy of this country if this country became, you know, for all of us, you and me, to be beholden to two service providers in telecom. I hope and I think the government and ecosystem will make sure there are more players.

Nikunj: Ok, closing comments. You spoke about this last time when we met. This is about you have explained it but I will revisit it as this is a questions which comes up at least on my twitter handle or a social media platform is that when markets realise that you are reducing your stake in your bank, and that's your personal stake, and at a time when the bank is going through a difficult patch, because of covid and transition. It just makes people wonder what is your skin in the game?

Mr. Vaidyanathan: So, why do you mention that I have brought down my stake. I still hold a substantial stake in the bank by my standards.

Nikunj: No, you have been selling shares for charity purposes. But I am bringing this point which people often write to us seeking an answer?

Mr. Vaidyanathan: The fact is that, you know, I had contributed about Rs 40 crore to charity at that point of time and later gifted Rs. 20 crores to few other things. See the fact is that my cash flow is salary and It is just enough for me to meet my personal needs. I do not have any more savings than that. So if anybody I want to support or help, I can only contribute only my stock to them. So, I know what you are referring to. Last quarter, I gave some stocks to a few people. None of my sale are for my personal take to myself ever, except the one which I did to square the loan in the Covid crisis. It's all for somebody else. Any case, my wealth is better if put to good use for someone else, than just being stuck in my demat account.

Nikunj: This is something which people ask on twitter handles to me to reach out to you to understand your thoughts behind it. I am glad, we discussed it again and you frankly spoke about it. Really appreciate Mr Vaidyanathan. Stay safe and certainly hope to see much more of you going forward?

Mr. Vaidyanathan: Thank you very much. I must point out to your viewers who are concerned about our profitability- since we did not talk about it. Because we are DFI, and you raised this question earlier also in a different context, Because we are a DFI, we are carrying Rs 27000 crore of borrowings even now from the pre-merger base and we are paying 8.5% interest on that. That is a drag on the P&L. That is why you find that our core pre-provision profitability is low, and when credit costs come, it shows in the P&L and all that. But once we pay off this debt, we replace it by less than 5%, you can see the margins sharply lifting. I will leave you with this comment.

Nikunj: Thank you for that and stay safe and thank you for joining us on the show.

Mr. Vaidyanathan: Pleasure talking to you.