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Synopsis

IDFC First Bank's CEO, V Vaidyanathan, discussed the impact of recent Tamil Nadu floods on their joint liability group loans, leading to higher provisions. However, strong deposit growth and diversified loan book are keys to their stable future. The bank aims to enhance profitability through a growing retail deposit base and effective risk management.

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IDFC First 2.0: 80% of deposits retail now; to touch Rs 6 lakh cr in 5 years: V Vaidyanathan

V Vaidyanathan, MD & CEO, IDFC First Bank, says massive floods in Tamil Nadu five or six months ago disturbed the joint liability group (JLG) portfolio. IDFC First has taken extra provisions on that book because people at the bottom of the pyramid suffer during a calamity as it affects their earnings and hence the capability to pay. We have taken extra provisions on that book but think of it like an episodic thing. It will go away in 1-2 quarters and probably even Q2 will have elevated provisions because of that reason. After that, it will taper off.

We were just looking through your JLG (joint liability group) portfolio, the intervention that you have undertaken, can you tell your shareholders what happened this quarter and is it more of a one-off sort or is there a risk or recurrence as well going forward?

V Vaidyanathan: From among 25 business lines, one of our business lines is the joint liability group business, it is about 6.3% of our loan book. That business is largely concentrated in Tamil Nadu there were massive floods in Chennai, Tamil Nadu five or six months ago. So that portfolio got disturbed. The people at the bottom of the pyramid suffer during a calamity as it affects their earnings and hence the capability to pay.

So we have taken extra provisions on that book but think of it like an episodic thing. It will go away maybe in one more quarter or two and probably even Q2 will have elevated provisions because of that reason. After that, it will taper off from there.

Historically, the microfinance part of the book has had lower NPAs but this time, because of the floods it may get elevated. Do you expect it to normalise in the next two to three quarters?

V Vaidyanathan: That is correct because our credit cost on the joint liability group business, for 18 months before the floods at a stretch was only 1.6%. After the flood, it has suddenly gone up and that is why we have taken provisions this quarter. It will stay elevated next quarter also. But these are episodes, they come and go but this business is very important to us because there are multiple kinds of priority sectors and we need the book lending to weaker sections and small and marginal farmers. There are many reasons we do it and also it goes well with inclusive banking.

How have you managed to grow the deposit so strongly at a time when the entire industry is feeling the pressure? What was the essence and what is the key recipe for this? How did you manage it?

V Vaidyanathan: We have been growing deposits very strongly for the last five years. Let me share with you that one of the key reasons: we are available to the media every quarter, announcing our results, and explaining the matters, and even if there is bad news we come and explain it. It builds trust. If it is good news, then it is good news. So, I think it adds to trust in the organisation. We are seen as an institution. It also makes a very big difference to be an institution and of course many other factors as well.

When you say that IDFC First Bank 1.0 was from December 2018 to March 2024 and from March 2024 onward, IDFC Bank 2.0 is starting. How are the foundations coming in place for this institution that you say you are building?

V Vaidyanathan: The foundation for 2.0 has been laid in 1.0. When we started 1.0, we had close to about Rs 78,000 crore of legacy borrowings which would come for repayment in the next four to five years and also, we had certificates of deposits – a very large number. So, during the foundation 1.0, we have raised a serious amount of retail deposits and we have paid off Rs 64,000 crore out of Rs 78,000 crore. So, now our credit deposit ratio has come below 100%. It was 160%. If you add back credit substitutes, meaning when you lend to a corporation in the form of bonds, that is also effectively credit. The credit deposit ratio has come down from 160% to less than 100%. So, we have built a very strong foundation in terms of retail deposit, branch network, etc. So, when you look ahead on this foundation of a good brand, good corporate governance institution, good image, and good fundamentals of credit deposit ratio, now for 2.0 we think the deposits in five years should be Rs 6 lakh crore, up from Rs 2 lakh crore at present and in three years, we expect it to touch Rs 4 lakh crore.

Not only have your deposits grown very well, but also there is a diversified liability mix. 80% is retail right now?

V Vaidyanathan: Yes, it was 23% retail five years ago, now it is 80%. We see this as a very positive thing because retail customers get are more sticky; they are used to internet ID, passwords, relationship, branch service, etc, so that is a really good development and we want to continue to grow our retail deposit franchise. It gives stability to a bank. Frankly, at 80%, we feel very stable.

In the basket of the loan book, I can see 25 business lines and none of the business lines have over 12% exposure. Tell us what kind of stability this brings and also the growth which we are witnessing on an aggregate basis.

V Vaidyanathan: Our concern was that if a portfolio is very dependent on infrastructure financing or corporate financing if you are just loaded on one, then any one item can move the profitability very much. Now it is 25 business lines. We have launched many in the last four to five years. Let me stick to assets; recently we launched gold loans, tractor loans, education loans and a large number of products. This just diversifies the book and brings multiple streams of revenue to the bank.

Infrastructure project financing is reduced from almost 19.5% to 1.3%. That is interesting. When we are talking about loan book growth, I want to go back about two to three quarters back. As a proactive measure, you had sobered down the guidance on the growth front. How is that panning out? Would you continue to stick to that loan book growth guidance which was slightly on the lower side to become much more sure-footed overall in the environment?

V Vaidyanathan: No, frankly, we were sure-footed even at 25%, but what happened was that for the first three years, we did not grow the loan book at all, very low at practically 5% or 6%. That was because at that time we had a big credit deposit ratio problem, so we did not want to grow the loan book. Then we started growing at a higher rate. Now, we have guided for more like 20-22%. This should be very easy in India because the market is so large and we are a relatively smaller player. So, it is not about growth. 20% is very easy. It is more about managing credit quality and that is more important.

This is an environment where certain sections are becoming slightly red-hot and the risk would start percolating in the books going forward. Up till now, you have maintained a very high asset quality of lower than 1.5% on GNPA and less than 0.5% on NNPA. Can you talk to us a little more about your risk management funnel, especially for retail, rural, and MSME, and how differentiated it is overall?

V Vaidyanathan: India is still in its early stages of credit. It is only 19% of GDP. There is a long way to go. So, the good thing is that in India itself, the ecosystem has come up even before the credit lending has started seriously in terms of credit bureaus and bank statements. Now, you can see bank statement details, you can see account aggregator details. So, the ecosystem of the country has become better and of course, we have a long track record.

We wear the fact that our gross NPA is 2 and net NPA is 1 as a badge of honour. We want to keep that badge of honour. We had a small skirmish in the case of joint liability group this quarter, but barring a small skirmish, we like the positioning of having a gross NPA of 2 and net NPA of 1.

Your retail, rural, and MSME product segments have very low NPAs. Technology of course is playing a big part. You are expecting comfortable risk management checks here. Are there any signs of a blowup or indicator going on the higher side in these three pockets?

V Vaidyanathan: We described that, actually in this presentation, we put out two curves in terms of a vintage curve. One is basically for the retail, rural, and SME, in these businesses, we had given the vintage of the past loan book three to four years ago and what it is for the post-COVID period and you can see that the new curve is like to like delinquency, take six months on books, nine months on books, 12 months on books at every vintage point, the new books are behaving better.

We should be very careful here because at the end of the day our headroom for, if you have to manage only 2% gross NPA, net NPA of less than 1, then the margin for error is very little. We share with our employees that we have no room for error, and we should be very careful.

You are also making a case that the profitability is likely to improve very smartly, especially the fee income, how is that behaving? Can you give us some colour on how one- to two-year can pan out on profitability and fee income front?

V Vaidyanathan: Our income core income is rising at about 25%, core income meaning the NII; our fees is rising by about 19%. So, income is coming very strong. Our operating is profit also, if I am not mistaken, about 25% or 28% is the increase in operating profit, so that number is coming quite strong.