What hasn't happened in past 50 years will happen in next five: V. Vaidyanathan

Capital First founder and executive chairman V. Vaidyanathan speaks at the MintAsia Global Conclave about reforms in India and its implications on small entrepreneurs

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Vaidyanathan says the whole ecosystem is ripe for banking with small enterprises today more than ever before because of digitalization.

The Competition Commission of India (CCI) has approved the merger between IDFC Bank Ltd and Capital First, the latter's founder and executive chairman V. Vaidyanathan said during an interaction in Singapore.

In a fireside chat at the MintAsia Global Conclave in Singapore on Friday, 9 March, Vaidyanathan, spoke to *Mint*'s Tamal Bandyopadhyay about reforms in the country—digitalization, demonetisation and goods and services tax (GST)—and how the changes have opened up huge opportunities to provide financing to small entrepreneurs.

"What has not happened in 50 years will happen in the next five," he said. "...the foundation has been laid—on this, you can not only do lending to small enterprises, you can also collect money from small enterprises and, therefore, the whole ecosystem is ripe for banking with small enterprises today more than ever before because of digitalization," he added.

Earlier this year, IDFC Bank and non-banking financial company Capital First had announced a merger of the two businesses to form a combined entity of assets under management of Rs88,000 crore and a distribution network of 194 branches. Edited excerpts:

Everyone wants to know why you are merging with IDFC Bank. IDFC's performance has not been that great. If you were looking for a banking licence, you could have waited. Why did you have to merge with IDFC Bank, especially since its (IDFC Bank's) merger with Shriram Group had been called off? And we see you stepping in as a white knight. So everyone is curious. Were you in a hurry to get a banking licence?

The straight reason is that IDFC Bank is a really good bank. Last two years, I think from the time it got the licence, there has been considerable progress—setting up the systems, setting up 100 branches, so they made progress. Now, yes, with regards to us, certainly I believe that we were looking for a banking licence for some time.

Capital First was founded six years ago, and our loan book had become Rs25,000 crore, and at some point of time, for an NBFC to keep growing beyond Rs50,000-60,000 crore would be a challenge, and some cycles can always come—liquidity and interest rate cycles. So, at some stage, we would have applied (for a banking licence)—maybe in a year or two probably.

But such an opportunity does not come often. So we just thought this was a good opportunity. We get, of course, a banking platform, we can sell more products. From their point of view, it was providential enough, a nice coincidence. They, too, wanted a retailization. So, together, I think it's a really big opportunity, and we probably will be creating a bank that is multiples of what it is today.

But what does IDFC get from Capital First? For IDFC, they have a reasonably large balance sheet on the asset side. But the problem comes from its liabilities. Primarily, it has been surviving, or rather, doing business on market borrowings. You don't bring liability to the table. You only bring assets. So, assets plus assets—where is the other side of the balance sheet?

Let's talk about what Capital First is bringing to the table. It is a very important question. You know, Capital First in the last 5 to 6 years has lent to 5.6 million customers—all ticket sizes are from Rs20,000 to about Rs1-2 crore. To access such customers in India—in a blue ocean—where 30% of the customers are not part of any credit bureau, they're first-time borrowers. To bring such customers and the ability to build such a base through all the new technologies we talk about—through Aadhaar, fraud detection capabilities, through banking technologies... That capability is what we have developed. Now, that is very important for IDFC Bank. With regards to liabilities, again an important question. Now, certainly, to be able to fund this sort of a balance sheet of Rs88,000 crore, probably growing from here, there is a need. I always take inspiration from the fact that if we are a \$2.3 trillion economy, and savings rate is 30%, then that's \$600 billion of savings coming into the country. If you take that forward 4-5 years, and you compound the \$600 billion, then that's a lot of savings coming here. Therefore, if we put up a branch network, have a good product proposition, if we reach the customers, and if we reach them through the new technologies which mean lower costs, then I have no doubt that liabilities will come.

So you are actually bringing to the table an infrastructure which can generate liabilities?

We are not bringing an infrastructure to generate liabilities. Infrastructure to create liabilities can be created. Today, there are 100 branches, and suppose we add 500 branches. End of the day, if we roll out a branch network, which we certainly think we will, there are enough customers in India who want a banking facility. So you will get the deposits. I have no doubt in my mind that India's got a large pool of savings and you'll get a hand of that bite.

You seem to be very passionate about small loans even though you are urban-based and mobile-based and living in Mumbai. You are into micro, small and medium enterprises (MSMEs) and SMEs segments and are continuously giving small loans to them. Where does the belief come from, and what's your vision on that particular segment—the missing market?

If you see the credit distribution in India— say India has Rs100 trillion of the market— of that, only Rs18 trillion is for the small enterprises. Now that's for, let's say, 50 million enterprises. And Rs40 trillion is for 4,000 corporates. India is like the bottom of the pyramid—the credit evaluation is built upside down. This does open up a huge opportunity. Second, with all these new sets of initiatives that have rolled out in India over the last few years—digitalization, demonetisation and GST—the ability to finance small entrepreneurs has expanded plentiful. What has not happened in 50 years will happen in the next five years.

Let us talk about digitalization. Is technology becoming a product itself, or will it continue to be an enabler in a country like India? Where does technology stand? Some of the Indian banks have started to say—or are tempted to say—"we also do banking", meaning they are positioning themselves as technology firms, which happen to do banking. Is that how you approach banking?
Technology is only as useful as the benefit that provides for the population. By itself, it has no meaning. What is happening in India is that a number of initiatives—let me say Jan Dhan, Aadhaar, mobility, artificial intelligence, credit bureaus—all of these things have suddenly come of age at the same time. Individually, they are important initiatives; but together, they are explosively beneficial to the ecosystem. Now, our belief is that, and we have held this belief for the last five years, and it has paid handsome dividends for us—the foundation has been laid—on this, you can not only do lending to small enterprises, you can also collect money from small enterprises and, therefore, the whole ecosystem is ripe for banking with small enterprises today more than ever before because of digitalization.

Why do you have to keep the government happy? Your approvals come from the regulator. Have you got clearance for the merger?

I am very happy to say that today (9 March), we got clearance from CCI. And we believe that the regulator is supportive of our efforts.

What is your biggest challenge? How can IDFC Bank differentiate itself from other Mumbai-based technology-friendly banks that aim at ease of transactions? Beyond that, what are the ingredients you need to bring to make it different?

There is no doubt that a large number of Indian banks are jumping on the technology bank bandwagon. We are not the only ones. I can certainly say that technology is there, but how we use it is of most importance. For example, there is Aadhaar everywhere—but a large number of banks are still taking physical KYC (know-your-customer) to still do the same thing. How do we use the Aadhaar, or AI? We believe we have taken a big crack at that.

Second, we are founded on technology—we are not a traditional bank that converted and then learnt to do digitalization. We started as a technology company and have lived and breathed that life all this while. Like I said before, I take inspiration from the fact that when people start talking about Indian economy becoming a $5 trillion one in the next 8-10 years, that additional $2.5 trillion is yet to be created. Nobody has a stamp on it—so, that is a new market. Nobody has touched it yet. We have a chance. We will create new credit markets, new liability markets and have a significant play in India which is yet to be created.