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Corporate distress needs some hard decisions

Five leading bankers say government spending is essential to revive growth and that banks are responding well to the technology-led disruption

What is your outlook on the economy?

Chanda Kochhar: I will take it at three levels: Macro economy, real economy and financial economy. If we look at the macro economy, we are in a very strong position despite the not-so-good monsoon and all the macroeconomic factors are looking much better today. Not just improved from the past but also much better when compared to the rest of the world. Our currency is more stable than that of other emerging economies.

On the real economy, we can see positive signs. For instance, Coal India's production has gone up. Overall mining activity is up. That creates movement of heavy commercial vehicles and so on. National Highways Authority of India (NHAI) is awarding contracts, and SME (small and medium enterprise) contractors are starting to get business. So these are some of the green shoots we are actually seeing.

In the financial economy, demand for car loans and commercial vehicle loans remains strong with 16-17 per cent growth. Demand is coming from SMEs and banks are lending. What we are waiting for is a revival in big investments. While the private sector is completing ongoing projects, the bigger investment push will come from government spends. The way things have picked up on the highway side, the next area will be Railways, where we have already seen some large contracts being awarded. After that we should see activity from the defence side. The bigger kick for the economy would come from government spends and, broadly, I think we are moving in the right direction.

Aditya Puri: Credit demand reflects the GDP growth rate and to some extent it is distorted in the way it is reported. With lending coming from mutual funds, etc., and considering that there is no oil demand on a comparative basis, credit demand will be 12-14 per cent. So that's not inconsistent with a stable economy. The banking sector is definitely not a constraint. There are fundamental issues outside the banking sector which need to be sorted out and there is no point expecting the banking sector to lead a recovery.

Arun Tiwari: If we look at the larger picture, the centre of gravity of GDP growth has been shifting towards the East. India and China contribute 50 per cent of that. If we look at the global ageing population, we are in a sweeter spot as out of the 1.36 billion of population, 800-850 million are below the age of 30-35 years. This is one set of population, that's aspirational and the economy has to do well to accommodate their aspirations.

Pramit Jhaveri: It is not fair to compare how the banking industry has grown in the last 20 years with how it is growing today. In the short-term, things are pretty good and in the medium- and long-term, there is room for great optimism. Coming to the segments we serve, it is unfair to look at only private corporate sector and generalise for the industry. Retail sentiment has been good over the last 18 months, and so have public sector and government spending. Also, India has been more integrated with the world in the last 20 years, and if the rest of the world is struggling, we can't be completely immune to it. If you put all of this together, there isn't much to be pessimistic about.

Ravneet Gill: If you look at it from the classical perspective of economic recovery you link it to the capex cycle, but there are many other factors that give you an indication of the health of the economy. Current account deficit, fiscal deficit, etc., are trending in the right direction. From an emerging market perspective, India is doing quite well vis-a-vis China. While all the large economies in the world moved from the manufacturing to services sector, India is now charting a path which has never been taken before of moving from being a services economy to a manufacturing economy. I am very positive on the economy over the medium-term.

We have seen a trend where foreign banks are withdrawing from specific segments from the Indian market. Your view?

Gill: There are two aspects to that. The costs of being global have gone up a lot. So if you look at individual jurisdictions and geographies, the cost of compliance and capital rent are going up. I think this has to come down. The second is, the international banking licence itself. Then you need to see your core strengths, which are scalable, and then you need to align in a global fashion. So sometimes sitting in India will feel you are missing a bus in terms of not investing in one particular business, but if you look at it from the point of view of the institution from the global level, then you can't be pursuing diverse strategies in different markets. From that point, it needs some recalibration of businesses. We need to assess the overall commitment in terms of balance sheet and capital, and whether foreign banks are reducing that in India. The answer is that the commitment of foreign banks remains undiminished.

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CHANDA KOCHHAR MD & CEO, ICICI Bank

"PSU banks have much higher NPAs. But did we think four years back that the economy will start doing badly? No. Do we believe that banking is a reflection of the economy? Yes. Growth can't come unless the core sector is fixed, be it cement, steel or power; here the cash-flow is the issue"

ARUN TIWARI CMD, Union Bank of India

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PRAMIT JHAVERI CEO, Citi India

Will foreign banks see their share of the total banking pie shrink over time and when?

Jhaveri: You have to look at it over a period of time, and see how a foreign bank in a segment does in terms of consistency and how Indian banks do. If you step back to the global financial crisis and what followed after that, a number of banks had to go through restructuring. Today, foreign banks are in a much better position to actually take advantage of markets and economies. There are some that didn't go earlier, but are going through restructuring right now. If you look at the physical presence the foreign banks have and the actual market share are very different. Market share is higher and I would like to believe that going forward if we play it right, we will be able to execute it consistently, there is no reason that the formula should change.

What about the whole disruption caused by technology?

Kochhar: Disruption will not happen because of technology being created or new forms of entities being created. Let us worry about what's happening in technology rather than getting worried about new forms of entities, because irrespective of different forms of entities coming up or not, technology is enabling things to happen and technology will change the way we all do business. Secondly, what has disrupted is business models and not businesses. As far as banks are concerned, their clients are living around digitisation, mobility and social media. It is important to keep offering what they need, and banks today are doing that.

A few banks such as ours are not just agile enough, but are moving ahead of the curve. In the past, a large part of our transactions were done through branches. Then there was a wave for ATMs. The current wave is mobile and internet. So today branches contribute less than 10 per cent of our transactions, whereas mobile transactions have increased substantially. Things are changing and technology is making it possible and consumers are responding to it. The banks too are clearly responding to it and they are making it available to consumers.

BANKING ROUND TABLE

Are you a technology company that happens to be a bank?

Kochhar: We are a company that provides banking service through technology. In today's day and age, banking gets provided through technology and you cannot separate the two. That's the way consumers want it and that's how it will be. There is so much of usage of technology even internally. Technology has a role to play in operations, data analysis, understanding the credit needs of customers and customer interaction. Technology has become a part of everything we do and we are on top of that.

Puri: Too much is being said about this. Banking is not changing. It is the business model and delivery mechanism that will change. You have to adjust to the advantages that technology offers to change your business model and the way you analyse big data and the information around your customers to provide far more focused products. So you look at all these disruptors, they are talking about making payments easier or making e-commerce purchase easier. So we split this into two; how can the network change your fundamental business model? And when we changed our model, we do a loan in 10 seconds for our customers and I don't think there are any disruptors who will match that. Technology only changes the way you manufacture, produce and deliver.

Are there segments of business that might be seriously challenged like credit cards, since mobile phones are getting more popular now?

Puri: Mobile wallets will only be for a certain set of customers, but cards and payment mechanism will only increase, that is why we are moving towards further dominance in the credit card business and intend to take our share to 40 per cent. So cards as a payment mechanism will exist whether it is loaded on wallet or as virtual card.

Mobile is only an enabler. The wallet is also loaded on to a mobile. We must distinguish between technology as an enabler and technology as a business. I told one of the telecom guys there, don't take telecom with banking.

Kochhar: Even if you take the mobile wallets, banks launched them even before the other forms of mobile wallets were growing. Banks have an advantage, for example, our 'Pockets' customers can load money to the wallet and use it; even those who are not customers can use the wallet. So the same service can be given to newer customers and to our own customers who want to use your product. Similarly, if everybody has to make payments through mobiles, why would they use other forms of payments? The point is somebody who is very comfortable using the mobile can still use the mobile app of the bank.

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RAVNEET GILL CEO, Deutsche Bank India

Will technology have an impact on employee strength?

Tiwari: Transition issues are everywhere. In the last five years we have seen the onset of technology in the banking space, but the number of branches have doubled. So there will be hybridisation of clicks and bricks, and they have to co-exist. It is more about the services and about whether I am able to create value for the customer. From a PSU bank perspective, in my bank, 63 per cent of customer-facing transactions are e-transactions which are one of the highest in this space.

Talking about cost implications, as of today, the officer's average age is 37 years, nobody would believe that. They come with those kinds of aspirations, this is a "140-character" generation. Gaps are there and we are taking care by bringing those skill-sets.

Foreign banks introduced new technologies in the system. But is the initial mover's advantage getting eroded?

Jhaveri: The banking industry has been acutely competitive. We have witnessed extraordinary amount of change. In the next few years, there will be competition from some non-banking players and the change may be faster. But that doesn't change the basics of banking.

If you look at the basics, what you really need is a focus on customers you will serve, your value proposition, ability to deliver it in a manner that they want, creation of economic value for them and finally, is a good experience that is simple, safe and secure.

Yes, customers may choose to do business with other banks, but that does not take away our value proposition.

Technology is embedded in the way we've been doing banking for 25 years in India. There are just different types of technology that we are referring to. It is only going to increase the size of the pie and make the life of a customer better but I don't think that it is going to be disruptive as long as we think of new ways like we traditionally used to do.

Private sector banks account for 30 per cent of the system while public banks account for 70 per cent. By 2025, how do you see those ratios changing?

Kochhar: Private sector banks have consistently been gaining market share and the trend will continue. A large part depends on individual banks' capabilities to grow, how far ahead you are in the usage of technology, competitiveness, capital adequacy, having a vast range of products which consumers use, ability to think through what are the growth areas and ability to participate in growth.

If you look at us as an example of a private sector bank, you have the people, talent, technology, capital, you have the ability to grow in whichever part of the economy that grows.

You cannot set growth rates for yourself, irrespective of how the economy grows. In India, banking industry should grow at least 2.5 times the GDP growth rate. In the next decade, we would grow at least three-four per cent faster than the average growth rate of the banking industry.

Private sector banks have been more careful in recent years while PSU banks have been quite aggressive. As a result, many in the latter category are also facing restriction in the ability to lend further due to capital adequacy norms. Do you see this accelerating growth of private banks?

Puri: Banking industry has tremendous opportunity; it is an under-served economy by organised finance compared to rest of the world. So the demand is not an issue. In that scenario, everybody will grow. But everyone has different business models, different target customers, different growth rates, profitability etc. We are very clear that we don't push the envelope. We have targeted a five-seven per cent higher growth rate than the market over the last 20 years and that has not changed.

People underestimate public sector banks, I think they'll come out fine. Will we grow five-seven per cent faster than the market? Yes. Will the public sector banks disappear? No.

Tiwari: Talking about growth, capital will not be a constraint. If we talk about our balance sheets and impaired assets, about 58 per cent is due to stalled projects. Growth can't come unless core sector is fixed, be it cement, steel or power, here the cash-flow is the issue.

Puri: There could be some consolidation as well.

Is Jan Dhan an opportunity?

Tiwari: Due to Jan Dhan, there is one realisation that the poor are also bankable. Everybody would benefit.

Puri: Let's not look at Jan Dhan in isolation. If you look at Jan Dhan, with Aadhaar and MUDRA, there is enough money at the bottom of the pyramid. We already deal with 4.2 million families below the poverty line and we are going to take it up to 10 million. We could even take it to 20 million if we had proper identification and there is consistency in subsidy payments. This would allow me to change my credit perspective.

It is also important that a lot of banks have not gone into semi-urban and rural areas — where 60 per cent of India lives — with their products even for the rich.

We are growing twice as fast in semi-urban and rural India than in urban India.

Some of the largest business houses in the country are laden with debt. There is also a commodity down cycle. How much of this worries you?

Puri: The groups in trouble are not the biggest groups in India. Maybe, one or two are big groups, but no one had heard much about them 10 years ago. And they are definitely not the biggest groups in the time I have spent in the Indian banking system.

But they have become big for the banking system...

Puri: Yes, for people who dealt with them...

Jhaveri: There shouldn't be sweeping generalisations. Yes, there are definitely some pockets of high stress and banks will have a challenging time, but I think making a sweeping generalisation across corporate India is unfair because that is not the case. In the last five or six years in India, the corporate side of our business has grown and we have lent more to our clients. Today, our non-performing asset (NPA) level on the corporate side is very low and we feel very good about it and we are in a position to continue to grow.

I think the only solution for those pockets of trouble are very hard decisions, a lot of pain and time. These are three things and you have to deal with it.

Gill: One of the things that one often says is that look at the level of ambition in China and look at the lack of ambition in India. A lot of these groups that invested in 2007-09 and beyond were thinking that India will continue to grow at nine per cent. And India didn't grow at half of that rate. This led to a lot of overcapacity. Many of these guys created assets. So it is not that the money disappeared.

The question is, could you still grow very profitably and keep your risk in control? You could. We met one of the deputy governors recently and he was wondering how did we grow at 20 per cent in this environment? Our NPAs continue to be absolutely where we want them to be?

So I don't think that everybody should be painted with the same brush. By and large, the big groups are in a reasonable state. With passage of time, they will get a chance to de-leverage. In the medium-term, though corporate India is not investing, a lot of cleaning up is happening. It will come with some degree of pain, but this will put, by and large, the Indian economy on a much firmer footing.

But current problems exist...

Puri: There are pockets that are going through a lot of difficulty. Some of those difficulties are not of their own making. They were told there would be raw materials and so on which did not materialise. While some can be turned around, others will have to take a very bitter medicine. Is the system capable of giving that medicine is the question? Given what the RBI governor and Ministry of Finance have been saying, I do believe so. Anyway, I don't think there is an alternative.

Tiwari: PSU banks have much higher NPAs. But did we think four years back that the economy will start doing badly? No. Do we believe that banking is the reflection of economy? Yes.

While NPAs have not stopped, the propensity of creating new NPAs has gone down.