Our Views

A conversation with Mr. K V Kamath

Last week The Economic Times held its Annual ET Markets Global Submit 2021 where I had an opportunity to host a session with Mr. K V Kamath, former Chairman of ICICI Bank and Infosys and former President of the New Development Bank of BRICS nations. His in-depth understanding of a wide range of issues and his visionary thought process, for which he is extremely well-known, prompted me to share his views through this article.

Focus on long-term sustained growth cycle

While the pandemic came as a shock last year, Mr. Kamath believes that a reset of the mind allowed Indian corporates to squeeze out productivity gains, not just at the shop floor level but in white-collar roles as well. Propelled by this change in mindset, we should now continue to work on efficient utilization of resources and improving quality of output. As a long-term strategy, the focus should be on two main areas – a right interest rate and right exchange rate environment, which has driven the recovery. Sustained low interest rates will promote demand in the economy and an attractive and stable exchange rate will boost growth. Japan and China had followed a similar twin-strategy of low interest rate and a stable currency to maintain long-term sustained growth cycle.

Furthermore, the Atmanirbhar scheme is a timely and positive intervention for the country as it comes at a time when we are ready for a mindset change. A scheme like the Production Linked Incentive Scheme (PLI scheme) could be a catalyst in this growth as we would need to sustain productivity and growth over a long period of time.

On the question of how to maintain a lower interest rate environment on a sustained basis, he believes inflation would indeed have a direct bearing on the same and it will be critical to control inflation. At the same time there is a need to consider whether an interest rate hike is the only tool. Also, given the link between inflation and fiscal deficit, it would be important to look at the true fiscal deficit situation, segregating developmental expenditure and other expenditure. Given that the benefits of developmental expenditure accrue over a long period and drive growth, I infer that the Government could look at different funding structures as has been done with NHAI almost like looking at two balance sheets for borrowing.

Banking sector

On banking, there were three key take-aways for me:

- The clean-up of bank balance-sheets had already been done over the last few years. We came into the pandemic, with fairly strong balance sheets and therefore there was not much of a residue to be addressed in the last one year. The anticipation was that the pandemic will result in significant stress on corporates and consequently on banking balance sheets. However, we do not really see that playing out. Corporate performance during the last two quarters has been better than expected and corporate loans do not seem to have deteriorated as feared earlier. We would need to watch retail loan performance over a few quarters.

  Of course, he acknowledged the assessment in the Reserve Bank of India (RBI's) Financial Stability Report earlier this month that said gross NPA ratio of public sector banks may rise by 650 basis points to 16.2 per cent by September 2021 under the baseline scenario. And, if the situation worsens, the ratio may rise to 17.6 per cent. It should also be noted that banks are waiting for the Hon'ble Supreme Court Orders.

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- On the future of the Public Sector Banks (PSBs), he believes that PSBs are going to continue being an important part of our banking system. Strong PSBs are required to meet our next five-year growth aspirations.
- In the context of bank balance sheets he observed that corporate balance-sheets are also stronger today and they are focused on reducing debt, as can be seen in the sharp reduction in debt-to-equity ratio of top 50 companies compared to the 1990s. This should be comforting for banks. India Inc has used profits to deleverage even during the pandemic. Probably for the first time in our economic history, corporates are generating enough cash to expand brownfield projects and fund greenfield ones, with only limited debt from outside. In the past, it was the other ways around. It is not that there will not be any pain in the immediate future or over the next five years. It's just that we likely know where those areas of pain are going to be, and gentle hand holding may be required.

Need for a new Development Financial Institution (DFI)

Having been closely associated with a DFI in the past and its later conversion into a bank, Mr. Kamath's views on the need and utility of a DFI or long term lender in the current context were very insightful. Post 1995, when the SLR status of bonds issued by DFIs were withdrawn, they had struggled to stay competitive and relevant. Hence, most of the DFIs converted into commercial banks over time. However, today, due to ALM concerns, commercial banks are unable to fund large long term infrastructure projects which is a prerequisite for economic growth. Hence, there is indeed a need for a long term lending institution. With the growth in insurance and pension sectors, concerns about long term liabilities are addressed.

Interestingly, Mr. Kamath's expectation is that industries which are born out of the digital super-cycle or which are leveraged by that super-cycle will contribute to at least one-third of the growth in economy over the next decade. New entities coming out of the digital era, like ecommerce or fintech players, are funded by equity and run by idea-driven leaders and would be huge contributors to growth.

Sunil Sanghai
Founder & CEO
NovaDhruva Capital Pvt. Ltd