

SEASONAL

MAGAZINE

BANGALORE DUBAI KERALA CHENNAI HYDERABAD MUMBAI

Monday, June 7, 2010

[Can Manappuram Keep Growing at 60%?](#)



For early investors of Manappuram (BOM/BSE: 531213), it has been a dream run. Celebrity fund Sequoia of Apple-Google fame has acknowledged it as its best India investment. The Kerala headquartered NBFC with gold loan at its core, is preparing for its third round of rapid growth. Will maverick entrepreneur VP Nandakumar follow the Kotak (BSE: 500247, NSE: KOTAKBANK) model, the HDFC (BSE: 500010, NSE: HDFC) model, the Shriram Transport (BSE: 511218, NSE: SRTRANSFIN) model, or their own Manappuram model to enter a higher orbit? The unconventional leader he is, Nandakumar is now betting on growing the gold loan segment to its real potential, rather than on other smaller concerns. Seasonal Magazine interviews Chairman Nandakumar and Managing Director I Unnikrishnan to find out whether their plans to keep growing Manappuram (BOM/BSE: MANAPPG) at 60% YoY for the next 6 to 7 years can deliver or not.

Who will believe that a pawn shop in a remote Kerala village will one day be audited by Ernst & Young, attract private equity from Sequoia Capital, and get featured in New York Times? Probably none, not even the most diehard entrepreneurs, as we associate E&Y, Sequoia, & NYT with the likes of Apple, Yahoo, or Google. But that is exactly what a Keralite by name of VP Nandakumar did, or, should we say that is what happened to VP Nandakumar. This is that unbelievable a story. Jokes apart, the Executive Chairman of Manappuram Group of Companies has had lots of both – what he did and what happened to him. Often, life packs its goodies in unfortunate incidents, and a young Nandakumar was thrust with the responsibility to run the family's gold loan business when his father passed away suddenly. Nandakumar was at that time an officer with Nedungadi Bank. A strange coincidence as it may seem, this bank ceased to exist as such shortly afterwards due to a crisis-led amalgamation with Punjab National Bank (BSE: 532461, NSE: PNB), and Nandakumar went on to do financial magic or let magic happen to him. In some ways this magic was in his DNA. His hometown of Thrissur, apart from its cultural leadership in Kerala, was famous for the finance business, being home to at least three banks – South Indian Bank (BSE: 532218, NSE: SOUTHBANK), Dhanalakshmi Bank (BSE: 532180, NSE: DHANBANK), & Catholic Syrian Bank – not to mention its status as the national capital of the chit business. Nandakumar's entrepreneurial greatness is that he believed in this DNA and this DNA's potential to elevate Manappuram from a village entity to a national entity. Today, Manappuram General Finance & Leasing, the Group's flagship and listed entity is an investors' darling, having gone up 500% in value since March 2009 lows, even while Sensex struggled to rise by barely 80%. His close associates will point out an uncanny ability in complex problem solving as his core strength, while Nandakumar himself would give due credit to the limitless possibilities of their core gold loan business in this country. Gold loan is the most secured of all loans, and thus has negligible NPAs. That eliminates the only risk from this money-minting business called personal financing that has one of the best yields in business. No wonder Manappuram's recent QIP garnered Rs. 245 crore from 12 high-profile investors including Nomura, Merrill Lynch Capital Market, India Capital Fund, Morgan Stanley Mutual Fund, & SBI Mutual Fund. Now after a stock-split and bonus issue, not to mention excellent results, the real question before Manappuram is the way forward – whether they want to follow the Kotak model, the HDFC model, or follow on their own model. Seasonal Magazine interviews VP Nandakumar for this cover story:

Manappuram has had a dream run since 2006, not only in the capital markets, but in fundamental growth. To what do you attribute this success?

The Manappuram story is, basically speaking, a story of realizing a hidden potential which is there in all of us. What I mean, specifically, is a funding potential. We Indians have this treasure called gold stored away in our cabinets and bank lockers. We even end up paying locker charges for it. But what is this material basically? This is just another form of currency, perhaps the most stable currency in these troubled times. In fact, in most of the developed world you can settle your dues in gold. But most of us have never thought about it that way. Manappuram tapped into this potential by focusing and growing our gold loan business.

But Manappuram has been in the gold loan business for long, maybe from the 80s. What happened in these recent years to witness this exponential growth?

Yes, but not from the 80s, Manappuram was there as a single-branch gold loan operation since the late 1940s. I took charge from my father – who was the founder – in 1986. The growth since then has never been symmetric. We had diversified into other typical NBFC activities like leasing and general finance. At some stages, we were less focused on gold. Meanwhile, we progressed on the incorporation front, moving successively from a proprietary concern to a private limited company to a limited company and then to a listed company through our IPO in 1996. But overall, two rapid growth phases stand out – one, between 1998 to 2006, and the second, 2006 to till now.

That also means, the going hasn't been that smooth always...

It was never smooth. Manappuram is a story that didn't just happen with the overall economic development, but a case that grew against economic adversities. In fact, all our turning points were adversity driven. This is one factor that I feel proud about, that this is in our DNA. Going forward, I think this is going to be our differentiating edge.

Can you describe how these adversities and subsequent growth phases happened?

Well, even before the two stages that I mentioned, there should be a few words. Leadership of Manappuram was not chosen by me, but almost thrust upon me when my father encountered a terminal illness. I was comfortably working as a probationary officer in a private bank then. I was not too keen to take this up, but did so after careful contemplation. This was not about a small family business at stake, as we could have easily wound up that over a short period. At stake was a values-based activity that my father had carefully nurtured, earning the trust of thousands of fellow villagers. The choice was before me – squander this trust, or realize its value and build upon it, however small it was then. Even to this day, we at Manappuram value this trust of our customers and other stakeholders above everything else.

So, the very beginning was in adversity...

That is what I meant. It was a risky jump, taking over the reins of Manappuram. But then the initial going wasn't as tough as I imagined. Luckily for me, the trust that my father had built up was enormous. In those good old days, even small financing companies like ours were allowed to take in customer deposits. But my father, the conservative person he was, had voluntarily limited his deposit and loan books to sub 25 lakh levels. Villagers used to queue up here, enquiring whether there is any slot for deposit, and my father used to keep a bunch of inland-letters ready for them, sending them one by one as some other depositors withdrew their money. That was the kind of trust he enjoyed. In the initial

years what I did was just to leverage this trust, by doing away with his voluntary limit on deposits and loans. The business quickly shot up above 1 crore, and then even beyond.

Still, Manappuram was a proprietary concern?

Yes, and that was a huge drawback for me. Remember, I was not hit with the entrepreneurial bug or anything, but I never forgot what I had forsaken to take this up. Here I was, once a well-travelled and accomplished corporate credit specialist at a bank, doing this 300 sq ft pawn shop. I decided that whatever I do, it had to be professional and excellent. I could always rely on this small operation's values and business logic, but I needed to create something much bigger and respect-worthy.

That must have been the beginning of MAGFIL?

Exactly. I looked around and found that Thrissur, or Kerala, for that matter didn't have much of a model to offer for financial companies. Most operations, for example those Thrissur based chit companies, were friends or family affairs. They were good at making money, but transparency was their last bother. I decided to do just the opposite. Instead of having friends or family members to occupy the Director Board, I created this company with accomplished financial and management professionals. The domains selected were general finance and leasing, which I thought will be highly productive areas. That is how our flagship NBFC, Manappuram General Finance and Leasing was born.

What made you go for its IPO? It was practically unheard of for a Kerala based company in those days?

Mainly, there were two reasons. All my efforts at having transparent procedures and good corporate governance at Manappuram were logically pointing to the next stage – the publicly listed universe – where such values were not only respected, but were the make-or-break factors. Remember, this was in the 90s, the age of Dr. Manmohan Singh's economic liberalization and the advent of respected operations like Infosys. So, there was a synergy. Secondly, I was fed up with raising money from banks. I had even put in my house and entire belongings to a local bank to raise money. But that kind of money – one or two crores – was not enough to fund the expansion plan I had in place for MAGFIL. A public issue appeared the most appealing way forward.

Apart from having a professional Board in place, what are the transparent procedures that you are mentioning?

There are so many facets to transparency. To mention just one, Manappuram is not only one of the largest income tax payers in its sector as well as in Kerala, but we have never had any serious dispute with IT department in our history.

How difficult was the IPO, especially with Manappuram put up at a remote village of Kerala?

Well, some things were easy, and some others quite difficult. Non financial aspects like accounts, transparency, governance, rating etc were non-issues for us. In fact, we were the first NBFC in Kerala to go for voluntary rating, at a time when most of our competitors were not even aware of such things. But the financial side was quite difficult. At that time, a company going in for the IPO should have had a minimum of Rs. 3 crore as paid-up capital. We were around half of that, 1.5 crore. So I embarked upon an initiative to collect small retail investments from among our customers, most of whom were from this village and personally known to me. This was a time when the kind of trust that I spoke about earlier came to our rescue. Still, many were sceptical. I assured them that I would take back their shares and pay them interest, in case things went wrong.

And did it go wrong?

You bet, it did! We were not ready for the dynamics of being listed at a stock exchange. We were listed at BSE in 1996. I used to watch in horror as our share prices slid from its face value of Rs. 10 to 9.5, 9, 8.5, 8, over the subsequent months. People who had subscribed to the shares before the IPO began queuing up for the promised buyback. Many thought that I wouldn't keep my word. It was so difficult too. But again, keeping their trust occurred to me as paramount. So, here I was, buying back Rs. 8 shares from whoever tendered it, and paying them Rs. 10 plus interest. Financially, it was the most foolish step an entrepreneur could take. But somewhere deep in my mind, I knew that it all could turnaround, provided we kept our faith.

These Rs. 8 shares were the same that went up to Rs. 690 recently, right?

Yes, they had appreciated by more than 85 times. But nobody had a clue back then. Many early investors kept their shares as I was advised that taking them back in such an informal fashion would amount to violating SEBI norms.

What do you think of the phenomenal rise of the Manappuram scrip?

From those early days, I understood that a business shouldn't be focussing too much on its share price. The only duty of the business was to grow its fundamentals stronger and stronger, quarter after quarter, year after year. The capital markets will take care of the rest. And that is what happened too. When we

shifted gears into overdrive, and our earnings started reflecting that, the scrip's price just went through the roof. As the stock market joke goes, price is nothing but P/E times E. Of course, when you start showing above-industry growth potential, you get rated at higher than industry P/E, reflecting your forward earnings.

We still didn't get to those two stages of growth that you mentioned...

Yes, the first break came in 1998. Better put, the first serious adversity came around that time. Government suddenly changed the rules of the NBFC game. Almost overnight, we were straddled with a serious asset-liability mismatch. It was almost the end of road for us. Many of my professional Directors fled. I had no idea whatsoever as how to go forward. I kept rethinking all my strategies, and finally the truth dawned on me. I had made a mistake by relegating the gold loan business. We were still doing this non-glamorous business, but on a lesser scale and under the old proprietary concern. I decided to bring that business into this company. Gold loans were not risky like other loans. They could solve my asset-liability mismatch to a large extent. Still, there was another headache – the source of funds. Just before the government changed its mind on NBFCs, I had made all arrangements for a massive expansion. My new branches were raring to go, and I had a new business model to offer, and no money.

How did you solve that finally?

That was the time when KV Kamath was having aggressive growth plans for the young ICICI Bank (BSE: 532174 NSE: ICICIBANK). One day I had an ICICI executive visiting me, and when they came to know of my healthy business model, they were willing to fund me to an extent. But the figure I had in my mind was ten times that. So he went back, and after extensive discussions at his HQ, came back with the idea of securitization, if I were to avail such massive funds. In those days, it was a novelty. Securitization involves transferring the gold loans from our books to their books, so that they could have a more trusted operation. I agreed and that is how this model, called ICICI Manappuram Model, was replicated by them elsewhere too. We could finally breath a sigh of relief.

Looking back, it was almost a miracle, isn't it?

Definitely. But such miracles happen when you are fully equipped for such fateful events. In our case, this preparation was our IT infrastructure. From my early days, I had invested heavily on technology. Information was, even back then, literally at my fingertips. I can talk on and on about transparency, but more effective would have been to see it in action. This is what we offered ICICI. With a click of a mouse, they could verify for themselves how a certain Manappuram branch somewhere in the country had fared that day. Built on the Oracle platform, today this networked software setup is equivalent to the CBS system recently implemented at banks.

But even with ICICI funding, your growth until 2006 was nowhere around your post-06 performance...

True, it was nowhere near. That point brings us to the second growth phase. Around 2006-07, ICICI Bank faced some regulatory hurdles regarding securitization, and they could no longer fund us. We were in an even bigger trouble. Buoyed by a few years growth, I had planned a larger-than-life branch expansion across the country. And when ICICI conveyed their difficulty, we again felt that end-of-the-road feeling. I decided to take a breather and went on to Singapore to present a paper at a conference of NBFCs. Again, a chance encounter happened. One of my childhood friends was then at Singapore working for Temasek, that country's sovereign investment fund. They were looking to enter the Indian financial sector in a big way, and through my friend they informed me that based on the paper I presented at the conference, they were interested in taking equity in Manappuram. After several rounds of discussions and due diligence here, and in Chennai, and in Singapore, that finally happened.

That also led to the scale up?

Yes, just like with ICICI, I had surprised them with my asking capacity. You can note that it is a special success trait that I am blessed with. Though they sanctioned only half of that, around Rs. 500 crore, it was a shot in our arm to go full speed ahead with our expansion plans. After the ICICI episode, I had also made up my mind to de-risk the entire operation, by never relying on any one fund source. Temasek's debt participation provided the visibility, and one by one, the others came, and we welcomed most of them. Celebrity PE funds like Sequoia, Capital World, and others.

What about the Indian response?

Some Indian institutions like HDFC Bank were quick to support us after this, following the foreign PE funds. But nationalized banks again proved difficult, even though we weren't too hungry for their support. But once SBI chipped in with a handsome infusion, almost all PSBs and the smaller private banks were eager to fund. Today, the situation is so favourable that I can pick up the phone and ask my CFO to arrange significant funds, even on an emergency basis. But we don't do that often as we haven't still availed almost half of our net sanctioned amount, and we are very particular now about the cost of funds. Still, arriving at this situation, after all those tough years, has been something of an achievement.

To what do you attribute this kind of acceptance among institutional investors, especially from abroad?

I think this has much to do with the post-2008 financial situation across the globe. Before the recession, it was a case of mindless financing. Post recession, institutions, especially from abroad are hunting for

secure financing. When they stumbled upon this gold loan business, they were pleasantly surprised. Here was the most secure of all loans – more secure than corporate loans, home loans, or vehicle loans. They were surprised to know that the major percentile of our loans were sub Rs. 20,000 and for periods as low as three months. Our NPAs are negligible, less than even 0.5%.

Going forward, what is the model you have in mind? Will you be working for conversion to a regular bank, much like Kotak Mahindra?

There was a time when I had my eye on the Kotak model. They were the first successful conversion of an NBFC into a bank. Owing to our good corporate governance and execution capabilities, we almost have an invitation to be a bank from some of the authorities. But nowadays we have realized that there is a better model to follow, especially if you keep shareholder value in mind. Compare what happened to Kotak and Shriram Transport Finance over the same timeframe, that is, after Kotak became a bank. Shriram could grow their assets under management much faster than Kotak. The reason is simple – while Kotak had to develop multiple competencies to succeed as a bank, Shriram became more and more adept at their core competence. A full-fledged bank has so many concerns like meeting priority sector targets and so on. Shriram's performance is all the more outstanding when you remember that Kotak's core skills was in financing new vehicles, while Shriram's continue to be the non-glamorous secondhand vehicle finance. Our core competence is in gold loans, and if we shed that to become a bank, our shareholder value may be eroded. It won't be good for our customers too, as now we are the masters of this service.

That still leaves another model to emulate isn't it? I mean the HDFC Bank model...

Definitely. That is one model that Manappuram Group is open to. HDFC could promote HDFC Bank (BSE: 500180, NSE: HDFCBANK) as a separate entity, each highly successful in their respective realms, and with no need to go for reverse-mergers like how ICICI and IDBI (BSE: 500116, NSE: IDBI) had to undergo. That model will also eliminate our concerns regarding diluting our ownership for the sake of being a bank.

How will be Manappuram's growth, going forward? Won't it be tough matching the last few years' performance? Don't you expect competition to catch up soon?

Manappuram expects to grow 60% YoY over the next 6 to 7 years. The principal reason is that only a tiny fraction of the nation's domestic gold reserves have been pledged so far. Coming to competition, yes, we expect some catch-up to happen, but again whether we will have distinctive growth solely depends on whether we can continue the innovation. You will be surprised to know that we were the first company in India to advertise a loan, back in the 80s. Yes, even before ICICI & HDFC. That time people thought that I was mad. Loans were things people begged for, not marketed before them, was the line

of thought then among banks and even NBFCs. Later, when gold loans caught up, we differentiated ourselves with tailor-made loan products. For example, using products, we addressed our main competitors, which were banks and individual financiers. One group focused on loan-to-value and other on interest-rate. So we created two families of products, addressing each, and thus catering to individual customer tastes. However, going forward, we will be focusing on enlarging the whole gold loan market, rather than creating a niche for ourselves.

That sounds interesting...

Yes, it is, and hopefully this will mark our entry into an even faster growth orbit. Today, gold loan still has a taboo in this country. For some it is the last resort, and for others it is not in their radar at all. But we believe that this is not fair on gold or its power. Many people, especially small-scale businessmen, go for funds from unorganized sector at 10 times or more interest rates than what we can offer them. Through a publicity campaign across the country that will feature celebrity testimonials, we will deliver this message – you have a power within, the power of gold, that you can decide to unleash. We have roped in stars like Akshay Kumar, Mohanlal, Vikram, & Venkatesh, to deliver testimonial ads about this hidden funding power of gold. We won't be asking the celebrities to endorse Manappuram, but to endorse this funding source. The objective is on growing the entire gold loan segment, and not on inviting customers only to Manappuram. We realize that no business can go on growing endlessly without increasing its social relevance. We have also launched gold-overdraft type schemes that can deliver better than what a few banks are offering through their Gold OD offers.

You have recently ventured into gold retailing. What is the motivation?

There are two reasons for this diversification. The main is that we could excel as an NBFC because we could rewrite the rules, thus paving for honest practices and good governance. Gold retailing is one such field where now honesty and professionalism take a back seat. We are confident that we can enter this game and rewrite the rules. We are applying our transparent accounting and good corporate governance in our gold jewellery business, with 100% BIS gold, and 100% billing. The company also expects to go for its IPO and get listed, by 2015. The other obvious reason is that owing to our background, we know too much about gold. That kind of knowledge is a comfort in business.

Are you planning any other diversification or expansion for Manappuram?

We are starting a new corporate office in Mumbai BKC, and a 60,000 sq ft new headquarters and data centre in Valappad, Thrissur. Personally, my other business interests include microfinance and affordable housing finance. As a Group, we have our eyes on a few sectors like equity broking, but nothing is finalized yet.

Born and brought up against adversities, do you expect a smooth ride for Manappuram Group?

No business can expect that. The rules and dynamics of businesses will keep on changing. There will be challenges emerging. But as a professional organization employing scores of CAs, ICWAs, MBAs, & Engineers, having a professional Board, and having a professional top leadership for which merit and performance are the only concerns, we are confident of overcoming all challenges. We don't intend to lose the trust of our customers, shareholders, associates, or any other stakeholders.

"Growth is in Our DNA"



Managing Director of Manappuram, I Unnikrishnan is a Chartered Accountant by training, and has been a Group veteran, having joined decades back as its first CA. This unassuming, seemingly light-hearted leader shares some rare insights into the Group's and its Founder VP Nandakumar's strategies:

Your Chairman states that you are brilliant. Do you share that view on him, and is it just because this is a mutual admiration circle?

No role for mutual admiration here. He only values merit, and growing up with him, I too have imbibed this merit-only value system. This is not only with me, that is how all the top leaders including our Joint MD, CFO, and others have evolved.

What do you find brilliant in Chairman Nandakumar?

His visions are always larger-than-life. And this has been the case when we were tiny, when we were small, and now when we are mid-sized. I am sure he will push on and think bigger, even when we are really big. That is what has been driving our growth. Thinking about other strengths, he is an excellent communicator, which as you know, translates to excellent marketing, and he is also extremely fast in thinking and execution.

How is he in delegating, grooming, empowering employees?

He believes in people, bets on them, and extends their capabilities. There have been so many examples here, even I am one. If someone is willing to run at his speed, Chairman takes him or her under his fold. But it is very challenging.

Being headquartered at a remote village in Kerala, which is more difficult – attracting talent or retaining talent?

Both are challenging. Attrition is not an issue at higher levels, but maybe at the entry level, which is the case at all companies. But we have created our own value propositions like sponsoring for MBA education. Growth prospects are also very good for performers as merit is the only consideration.

Will Manappuram remain at Valappad or are you moving to Mumbai?

You heard right, we are creating a corporate office annexe at Bandra Kurla Complex in Mumbai. But this will remain. In fact, we are creating a new headquarters cum data centre here. It will span eight floors and 60,000 sq ft, will be centrally air-conditioned, and will be the command and control centre integrating our 1100 branches across the country.