"Northern Arc Capital Limited

Q3 FY25 Earnings Conference Call"

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MANAGEMENT: **MR. ASHISH MEHROTRA – MANAGING DIRECTOR AND CHIEF EXECUTIVE OFFICER – NORTHERN ARC CAPITAL LIMITED**
MR. ATUL TIBREWAL – CHIEF FINANCIAL OFFICER – NORTHERN ARC CAPITAL LIMITED
MR. PARDHASARADHI RALLABANDI – CHIEF RISK OFFICER – NORTHERN ARC CAPITAL LIMITED
MR. CHETAN PARMAR – HEAD INVESTOR RELATIONS – NORTHERN ARC CAPITAL LIMITED

MODERATOR: **MR. CHINTAN SHAH – ICICI SECURITIES**

Moderator: Good day, ladies and gentlemen. Welcome to the Northern Arc Capital Q3 FY25 Earnings Conference Call hosted by ICICI Securities Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this conference, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is been recorded. I now hand the conference over to Mr. Chintan Shah from ICICI Securities. Thank you and over to you, sir.

Chintan Shah: Thank you, Dorwin. Good evening, everyone, and welcome to the Q3FY25 Earnings Conference Call for Northern Arc Capital. We have with us from the management, Mr. Ashish Mehrotra, MD and CEO and the senior management team. I would like to congratulate the management on a steady set of numbers. So now without further ado, I would now like to hand over the floor to the management. Thank you and over to you, Ashish, sir.

Ashish Mehrotra: Thank you, Chintan. Thanks, Dorwin for putting this together for us. Good evening, everyone. Thank you for joining today evening. I know it's Valentine's Day but thank you for taking the time out to join us today. We'll talk about the Northern Arc performance for the third quarter and first 9 months of the Fiscal Year 2025.

Northern Arc has built a robust and well-established distribution network over the past 15 years, which includes widespread presence in about 373 branches, a customer base of about 1.9 million and partnerships with over 343 originators with over 1,100 investors. The extensive network has enabled us to facilitate credit financing, totaling to over INR 2 trillion and impacting the lives of over 115 million individuals and businesses.

That being said, our assets under management have grown by about 16% on an year-on-year basis, reaching INR12,250 crores compared to the rather muted growth we've witnessed in industry. A proactive risk management strategy enabled us to anticipate and assess the stress emerging from the MFI space. As a result, our share of direct MFI exposure has decreased to about 9.6% in December 2024, from 14% in December 2023.

Furthermore, our diversified business model provides us with the flexibility to adjust our sectoral exposure or the exposure to a select set of customer segments as needed, allowing us to efficiently scale up or scale down in response to the opportunity or challenges in the marketplace. The current credit cycle is not something we are unfamiliar with. We have been cautious with risk management at the core and emphasized focus on risk monitoring and collections, both in terms of arresting flows and improving recoveries in case we are dealing with these stress situations.

Having said that, over the last 15 years we have weathered multiple cycles including events such as demonetization IL&FS crisis, DHFL crisis, COVID pandemic 19, while remaining consistently profitable quarter-on-quarter for 60 quarters. Our robust and diversified business model has enabled us to navigate these challenges while consistently developing the top quartile results on a quarterly basis.

The increase in GNPA is primarily attributable to the stress in the MFI sector, which as I mentioned earlier has been significantly scaled down. Further, as market conditions evolve, we remain cautious, and we expect that over the period of the next few quarters the market will tend to reach towards normalization. Apart from lending, we have a strong fee franchise, which essentially constitutes two parts of what we do.

One is the placement solution and the second is the fund management business, which provides consistently sticky fee incomes and provides a kicker to our return on assets. Our placement volume for the first 9 months is over 8,000 crores and compared to the same period, it's largely flattish because of the challenges I spoke about earlier in the MFI space. As the credit market stabilizes and the confidence returns, we anticipate resurgence in demand for the placement services, enabling us to regain the momentum and continue supporting the growth of flow of credit to the underserved and the unserved sectors broadly around the credit markets. I just want to clarify that on placement we don't take any risk on our balance sheet. This is purely the placement of structured financial solutions we provide.

On our performing credit funds, our AUM of INR 2,800 crores, with an additional undrawn commitment of about INR 350 crores coming within our existing funds. Furthermore, we've launched the climate fund, which we spoke about earlier, based out of GIFT City, which targets about $125 million. Today, we have a secured hard commitment of over $65 million from various foreign institutions. This commitment provides us with a robust pipeline to deploy approximately INR1,300 crores in the coming quarters.

The key differentiator to our growth strategy and to our overall strategy is strong technology and data analytics capabilities. We've built a strong proprietary tech platform like Nimbus, a loan origination system, nPOS, which provides on-lending and co-lending solutions, and NuScore, which is the proprietary score card and analytics platform.

Altifi, a distribution platform, has been designed to democratize the retail participation in the credit space. We expect to monetize these platforms in the coming quarters and years by collaborating with our originators and investors.

Our disciplined approach to risk management and strategic expansion has driven and delivered 22% growth on a year-on-year basis in our PAT, reaching about INR 267 crores for the first 9 months of the year, with a return on assets (ROA) of about 2.9%.

This period is reinforced with an important insight that a resilient business with a proven track record thrives in challenging environments. Our ability to navigate uncertainty while sustaining growth highlights our maturity, agility and commitment to value creation. Looking ahead, we remain focused on delivering the solid and sustainable performance of our business and creating a long-term value for all the stakeholders in our ecosystem.

I'm going to request my colleague Atul Tibrewal, our CFO, to walk us through financials, and then we can open the call to take the Q&A session. Thank you, Atul. Over to you.

Atul Tibrewal: Thank you, Ashish. Good evening, everyone. Thank you for joining the Northern Arc Earnings Call. Let me take you through the financial performance of the company. The asset management stood at INR12,250 crores, reflecting a strong growth of 16% year-on-year and remained flat in comparison to September 24. In terms of AUM mix, the MSME finance contribution increased to 39%, followed by consumer finance at 29% and MFI at 19%.

Our direct-to-customer mix improved significantly to 52% of the AUM. Our net revenue, including fees and other income, reached INR289 crores in Q3FY25, reflecting an 8% year-on-year growth. The interest accruals on write-off and Stage 3 loans amounting to INR 24.8 crores have been reversed in Q3 FY25. Fees and other incomes remained range-bound at 0.7% of the average total assets.

The cost of funds have increased marginally from 9.1% in H1FY25 to 9.2% in 9MFY25, due to liquidity constraints and the elevated interest rate environment in the market. Additionally, we have made significant progress in strengthening our balance sheet, with our debt-equity ratio improving from 3.9x in March 24 to 2.5x as on December 24. Our provisioning coverage ratio is at 60%. Our pre-provisioning operating profit or PPOP as we call Q3FY25, increased by 9% Y-o-Y to INR176 crores. Barring the set adjustment of interest reversal, PPOP has grown by 24% Y-o-Y to INR201 crores. Opex ratio was stable at 3.5% for the quarter.

Recognizing the overall ongoing stress in the MFI industry, we have strategically moderated our direct microfinance business. Credit cost in Q3FY25 is INR81 crores, which denotes 2.5% of the average total assets. GNPA and NNPA stood at 0.90% and 0.37% respectively.

On the liquidity front, we remain quite comfortable with positive cumulative mismatch across all time buckets. We had surplus liquidity of close to INR500 crores as on December 31, 2024, and undrawn sanctions of over INR1200 crores from various banks. Our total borrowing at the end of the quarter stood at around INR8,600 crores with approximately 65% tied to variable interest rates. So, these positions will serve us favorably to benefit from the anticipated lower interest rate environment in the future. We have also diversified our funding mix significantly during the year with an offshore fund raise of close to INR115 million in the beginning of the year which of course is on a fully hedged basis.

Capital adequacy continues to be strong well above the regulatory requirement, with capital adequacy standing at 26.1%. This provides us with enough headroom for us to grow our balance sheet for the next 2 years, 3 years. Our tangible net worth as on December 31 was INR3,405 crores. We made a PAT of INR76 crores for the quarter. For 9MFY25, PAT was INR267 crores, reporting a growth of 22% over the previous year. Thank you so much. With this, I would now like to open the floor for questions and answers.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Renish from ICICI. Please go ahead. Renish, your line has been unmuted. You may proceed with your question. As we are not getting a response from the current participant, we will proceed to the next question, which will be from the line of Nidhesh Jain from Investec. Please go ahead.

Nidhesh Jain: Thanks for the opportunity. Can you break down the credit cost on the direct microfinance portfolio and the rest of the portfolio?

Ashish Mehrotra: Sure. Our CRO Pardhasaradhi will take this.

Pardhasaradhi Rallabandi: Out of the overall credit cost of INR81.3 crores for the quarter, the microfinance portfolio credit cost is INR21.5 crores.

Nidhesh Jain: This is the direct microfinance. Direct microfinance portfolio credit cost is INR21 crores?

Pardhasaradhi Rallabandi: Correct.

Nidhesh Jain: Secondly how do you see the growth in the fund business over the next couple of years?

Ashish Mehrotra:

Ashish Mehrotra: I think we are reasonably bullish in our funds business. We have demonstrated with 12 funds performance over the last 9 years. We have successfully exited 6 out of 12 funds. We delivered better than promised returns in each of our funds and that shows the resilience and performance of the fund. If I look at an aggregate basis, the funds have delivered over 14.5% returns over the last 9 years on the fixed income platform. We are expanding our funds business.

The Climate Fund is the 125 million US dollar denominated fund is getting launched. We are finally on the verge of closing out our emerging corporate business fund where we will deploy close to INR1,000 crores and then we are in the process of launching three more new funds, which all being in the pipeline both in regards to the India Impact, 2X Fund, essentially supporting the online businesses and the second version of the emerging business fund, closer to the private credit.

Given the robust origination and the risk management practice, the fund business is poised to grow significantly from where it stands. We remain deeply committed to building that franchise given the track record of 9 years performance with over INR10,000 crores of deployment in the funds business.

Nidhesh Jain: Sure. What is the status of Aviom housing, which I think you have exposure to? Is it still current or have you classified that as GS3?

Pardhasaradhi Rallabandi: Hi. We normally don't comment on the status of individual exposures and measures taken to address risk issues from the portfolio. We have a framework for identifying the stress early, taking mitigation actions to minimize the potential losses, recognizing the staging of assets as per accounting norms and providing protection for losses early.

Provisions for this quarter include all the assets which are under stress or potentially under stress and discussed with our statutory auditors and approved by the audit committee and the board of the company. This is not the first time Northern Arc has seen a credit stress environment both in terms of retail and in terms of intermediary retail exposures. We have handled multiple stress situations on multiple cycles, whether it is demonetization or COVID or IL&FS crisis or any of these cycles.

We have a mechanism to handle both retail and intermediary stress and the process is continuing. I would not be able to confirm provisions on a specific asset.

Nidhesh Jain: Sure. Okay. Thank you. That's it from my side.

Moderator: Thank you. The next question is from the line of Renish from ICICI. Please go ahead.

Renish: Hi. First of all, congrats on a good set of numbers especially in the environment where most of the guys having MFI exposure reporting losses. It's encouraging to know that we have maintained our profitability. Sir, just two questions from my side, one on the borrowing side. So, when we look at the 9-month FY25 cost of borrowing sort of remaining at 9.2%, especially when we look at the bank's MCLR rates, it keeps on increasing. So how are we managing our cost of funds in this quarter and what is the outlook? I mean, given the rate cut has already started, how are we placed in the following rate cycle?

Atul Tibrewal: So, you correctly mentioned Q2FY25 were a bit tight in terms of liquidity. We did see the short-term rates go up. Few of the banks did increase their MCLR, but the good thing we did Renish, was that we raised sufficient amount of liquidity at end of September 2024. And we also raised INR500 crores of equity capital in Q2FY25. So today we are sitting on a good amount of liquidity, considering growth was a bit muted in Q3.

We are actually now seeing some of the rates coming down, both in the short-term and long-term. We are also seeing that the rates being charged by banks have also started stabilizing. So, going forward, we will definitely see some improvement or some reduction in the cost of funds. We continue to hold a good amount of liquidity that gives us a good cushion.

As I mentioned that 65% of our rates are variable and when we actually see the banks bringing down the rates post the repo rate cut, that should actually significantly help improve our cost of funds.

Renish: Got it. So, sir, let's say 64% of our borrowing with banks, what percentage of this is linked to EBLR and let's say, 1 month, 3-month MCLR?

Atul Tibrewal: Yes, most of it will be linked to MCLR of the bank, but close to 5% would be linked to repo rate. So, there also the change doesn't happen overnight. The change will happen at the end of the quarter, beginning of next quarter, but yes that's a very small amount of the total borrowing, but the major part is linked to MCLR.

Ashish Mehrotra: One thing I want to add is that the structure, the way our liability profile is designed, the long-term borrowing would be offshore and the amount of liquidity we sit on we probably will benefit significantly and more importantly, we have always had positive matches. So, probably among the NBFC peer groups, fair to say we will have one of the strongest liability franchises.

Renish: Got it. And, sir, maybe just a follow-up on that. So, offshore funding, a fully hedged cost is similar to 9.2% or slightly higher?

Atul Tibrewal: No, actually lower. So, we would have availed it at the beginning of the year. So, the rates were lower at that point in time, and we have raised $115 million So, the all-inclusive, fully hedged cost was less than 9%.

Renish: I see. Okay. And, sir, my second question is about microfinance exposure. So, it clearly mentioned that we have calibrated growth in this segment and I think this is the right strategy considering the current environment, but what is your internal assessment on the MFI? I mean, is it fair to assume that the asset quality has picked out and maybe from Q4 onwards we should start seeing the improvement or do you feel otherwise?

Pardhasaradhi Rallabandi: Yes, we have, as we have been seeing in the market and from all the disclosures from various participants, credit stress in the sector is quite high. In terms of what we should expect as credit losses from this portfolio, the way we look at it there are reports of some early improvement in delinquencies and very early bucket.

Renish: Sorry, sir, I'm not able to hear you, sir.

Pardhasaradhi Rallabandi: While we have heard reports and we have seen some numbers in some geographies of improvement in early bucket delinquencies, which might be seen as a turnaround after cycle, we believe it's a bit too early to call that, particularly with actions happening in various geographies in the last few days. One needs to be cautious in this environment and it's a little too early to call taking out stress in microfinance. We should expect some more months required for the financials to stabilize and credit losses to stabilize.

Renish: Got it. And, I mean, are you referring to the Karnataka bill or is it something else?

Pardhasaradhi Rallabandi: Yes, that is what I meant. While the notification clearly is not covering the regulated entities RBI regulated entity whether it is banks or NBFCs. We have to see whether there will be any spillover effects on the collection efficiency for all that.

Renish: Got it. I mean, if, sir, just a last follow-up on that, so if one has to exclude the Karnataka both in terms of the event and the collection, then the rest of India has started showing improvement or it is still, I mean, as you said, we should wait for a couple of months?

Pardhasaradhi Rallabandi: If we are talking about the credit cost or the NPA level, we should wait for a couple of months more. Collection efficiencies have shown little improvement, particularly in the month of December, but again 1 month of collection efficiency improvement is not something that we would like to go by. We would want to see a couple of more months of stabilization to be confident of that.

Renish: Got it, sir. Okay, sir. That's it from my side, sir and best of luck.

Moderator: Thank you. The next question is from the line of Paresh from Canara HSBC Life. Please go ahead.

Paresh: Good evening, sir. Sir, as I can see your Stage 2 and Stage 3 has increased by 40 basis points each from September to December quarter. I just wanted to understand that the increase in this stress is largely from MFI or also there are some exposures to your NBFC value line that have also been recognized in this increase in Stage 2 and Stage 3?

Pardhasaradhi Rallabandi: **Yes,** the increase in Stage 2 and Stage 3 is coming from both our intermediate retail and direct retail portfolios and not just from MFI.

Paresh: Okay, sir. All right. And, sir, your PCR has dropped quite sharply on Stage 3 from September to December quarter. I mean, where do you see this number stabilizing? Do you want to increase your coverage on Stage 3 and how will the credit cost look ahead?

Pardhasaradhi Rallabandi: Yes. Stage 3 PCR obviously with the sort of diversified portfolio that we have. Stage 3 PCR is a function of the mix of assets in Stage 3. If you have a secured asset, if you have a secured retail loan, say, if it moves into Stage 3, obviously because of the collateral value your PCR requirement would be lower. If it is unsecured, obviously it will be higher and in the case of unsecured retail loans we do write off. So, to that extent, there is no change in provision policy for Stage 3 assets whether it is institutional or retail. It is just a function of the mix of stage 3 assets

Paresh: So, if you have to give a breakup of your slippages in the quarter between the direct lending and your indirect lending, what will be the breakup roughly, sir?

Pardhasaradhi Rallabandi: Close to 25% of the credit cost in the quarter is from intermediate lending and the balance is from direct retail.

Paresh: No, sir. I was asking with respect to slippages and not with respect to credit cost. To increase whatever stress we have seen in this quarter, if you have to break it up between direct and indirect, what will it break up approximately?

Pardhasaradhi Rallabandi: It would be in a similar ratio. That's how the credit cost also has come, but I would have to come back with specific numbers on that.

Paresh: Also, sir, given that we are seeing a lot of stress in MFI and most of the entities are reporting losses, and we do a lot of lending to MFI institutions, how confident are we with respect to the asset quality in those exposures given that most of them would have to raise funds because of the losses we are seeing? And if we are having any exposure to unlisted entities, is it going to be very challenging for them to raise funds?

Pardhasaradhi Rallabandi: Our exposure to MFI in intermediate retail is only 10% of our overall balance sheet. The way we actually look at these numbers, I mean, while we are getting the perception is there that we lend to a lot to MFI, which is not true. We do, but in terms of the overall balance sheet size, our overall exposure to the microfinance sector is 19%, of which the direct piece is close to 9% and the balance is institutional.

There is a mechanism for us to evaluate the entities. There are internal ratings, but we are trying to check the entities. We are closely monitoring the risk. The way we look at it, as of now institutional space in intermediate retail and microfinance, we have not yet seen any entity getting into stress to the extent that we should be concerned about. We have a robust early alert and risk monitoring sort of mechanism, which continues and does its job, but no intermediate retail specific exposure that we are particularly concerned with now.

In fact, you were aware of the RBI action in the last quarter in terms of stopping new bookings of loans for a couple of MFI entities, both of which have actually come back. To that extent, in the intermediate retail space the scenario actually has slightly improved, obviously, while the retail microfinance portfolio continues.

Paresh: My last question, sir. How are you looking at the credit cost in the next subsequent quarters? Do you expect this number to increase materially from here or are you expecting it to be at a similar level to what you've seen in the first two quarters and third quarter?

Pardhasaradhi Rallabandi: We would not provide any specific guidance in terms of the numbers etcetera, but if you look at it the stress environment in microfinance and MSME sort of sectors is continuing, and we should be cautious and expect elevated credit costs for some time to come. Obviously, the earlier we are able to see the plateauing and improvement in credit costs, the better it is. We are looking forward to that, but it's too early to call it the top or to say that in one quarter it will come down or two quarters it will come down.

Paresh: All right, sir. Thanks sir.

Moderator: Thank you. The next question is from the line of Sumit Bhalotia from MK Ventures. Please go ahead.

Sumit Bhalotia: Hi. Thanks for taking my question. On the credit cost, I just wanted to ask you have mentioned already, but still wanted more clarification. On a quarterly basis sequentially, I see credit costs going up marginally only from INR78 crores to INR81 crores and you have also mentioned that you have taken the hit of the affordable housing fraud that has happened. Can you just help us understand Q-o-Q MFI stress has gone up and we have also taken this housing stress and still our credit cost has not gone up. That is one.

Second is on the MFI stress, I understand you have mentioned multiple times, but still direct to consumer, direct borrowing that we do in MFI, if I look at the entire spectrum of other companies which have reported, the credit cost is in the range of 5% to 15%. So, for us what is the provision that we have taken on the MFI book in the 9 months, and how do you see that pan out for the full year and next year, if you can share some numbers.

And lastly, on your direct lending, if consumer segment-wise break up on credit outlook, if you can give some insights into how the credit cost would be in different segments, that would be helpful?

Pardhasaradhi Rallabandi: Right. In Q3, we have actually seen an increase in credit cost. As Atul had mentioned earlier in the call, we have actually reversed interest on written off and Stage 3 assets which gave us some amount of cushion on the credit cost. Otherwise, if we have not made that change in the way we write back the interest in NPA loans, the credit cost would have been higher by INR24 crores.

Ashish Mehrotra: Income and credit cost both would have been higher by INR24 crores if we had not made that change in the way we calculate. So, to that extent, credit costs have actually gone up during this quarter. In terms of microfinance, as I mentioned, on the retail direct microfinance space we have seen an increase in credit cost.

And on the institutional space, as I mentioned again, there is a strong risk management mechanism and the risk monitoring mechanism that we have and the entities through which we provide these intermediary loans are robust and there was no requirement to provide additional exceptional credit loss provision in this space. To that extent, that was not really much of a concern.

And the third piece in terms of where we've seen consumer finance credit losses continue to be in the same range as they used to be over the last 9 months. In fact, it has only slightly come down. Microfinance is something that we are currently watching and there are some comments in terms of it being seen by November and December that are something we are still monitoring. Particularly, we would want to see each other for at least a couple more months, including Karnataka.

In fact, MSME stress levels also are actually higher during the last 6 months, particularly the unsecured MSME. Basically, what we call it unsecured business loans, but that is something that I think a lot of people have factored in, in terms of the pricing of the asset. To that extent, there should not be any extra price, whereas microfinance is probably not priced to this extent.

Atul Tibrewal: Sumit, also to add to your question on the 9 months credit cost for microfinance. Of the total INR211 crores of credit cost, around 25% would be from the direct microfinance business activities.

Sumit Bhalotia: Okay, that's helpful. Thank you.

Moderator: Thank you. The next question is from the line of Sushil Choksey from Indus Equity Advisors. Please go ahead.

Sushil Choksey: Ashish, first question is, what is the total consumer base between microfinance and other products we service directly and indirectly?

Ashish Mehrotra: So, we serve about 19 lakh customers, Sushil ji, directly through our network of direct lending businesses.

Sushil Choksey: And if you take a partner?

Ashish Mehrotra: This includes where we lend in conjunction with many of our lending partners.

Sushil Choksey: And historically, you would have served how many customers?

Ashish Mehrotra: We've historically impacted about close to 115 million lives. So, we've historically impacted a large number. We have about 40 million plus time series of loan performance data. So some of our scorecards and the work we do are significantly superior. That's the comment I made.

Sushil Choksey: Can you elaborate a bit on your scorecard?

Ashish Mehrotra: Yes.

Sushil Choksey: Elaborate a bit on your scorecard?

Ashish Mehrotra: So, we run over 22 plus scorecards in our models including for securitization and all the tools we finance and for our direct lending across the segments of consumers, small business loans, and all the loans we provide.

And these scorecards are built both looking at the leading data and the lagging data, which helps us to essentially identify the better cohort of performing loans and give us better outcomes. These are what we see if we would have run the score. So, I think the scorecards are a strong performance. We also bring in to offer some of them to other partners.

Sushil Choksey: You've generated historically and today so many million customers. Other than marketing, whether it's a housing loan, MFI loan or any other product which you're selling to your partners, direct consumer products which like any other banking partners are we tied up with any product, whether it's mutual fund, insurance or distribution of any product, which can be a big game changer in terms of fee income?

Ashish Mehrotra: Yes, so we are doing various things. One, we offer partners to pass their origination to banks and help them to originate loans. We are aligned with South Indian Bank. We are now working through to go live with three other banks which are Karnataka Bank and DCB Bank. There is one more PSU, which signed up last week. The advantage the partner banks have is that they can originate multiple types of loans, secure, unsecured, personal loan, business loan, gold loan, vehicle finance, affordable housing loans, loan against property. All these types of loans can be seamlessly processed using nPOS platform. We use nPOS, for our own underwriting and origination. On any given day, we underwrite, connect, approve and disburse over 25,000 loans a day. Probably the most robust technology and database solution for you to do KYC, penny drop, validate, run scorecard and approve a loan. So that's the one piece that we'll add as we go forward like the comment, I made in monetizing both the data and thinking curve.

The second is a platform called Altifi, which is also an RFQ registered platform, which was created to democratize the securities we have on our platform. And we've been down selling.

Now we are expanding that to offer other solutions, including over a period of time, mutual funds and other products.

So, I think that expansion will essentially net-net will be a high-quality lending business coupled with a very unique fee franchise. So, fee franchising coming from placements, funds business and from data sets. This is a pretty unique combination for any other non-bank finance company. I think that gives us the massive edge over a period of time.

And today, even on a challenging time, the fee franchise will make almost 70, 80 basis points of our return on assets. And as we see it expanding and growing quarter-on-quarter, we believe it should start providing the incremental kicker to the return on assets today. Thank you so much.

Sushil Choksey: Your platform is integrated with three banks as of today live that is South Indian, Karnataka, and the third PSU Bank?

Ashish Mehrotra: South Indian Bank is live. They have underwritten over, close to INR500 odd crores of gold loans coming from a very high-quality bank-based partner. We are integrating seven other partners there. And DCB and Karnataka Bank, we are integrating right now, so hopefully it should go live by the end of this quarter.

Sushil Choksey: Do you retain any part of the portfolio books or it's 100% correct?

Ashish Mehrotra: We make the cash income on enabling the flow of credit. The fee income is a component of two parts. For long-term loans, which are essentially more than 24-month loans we earn annually, it is the average net receivable of fee. For short-term loans, which are less than 24 months of debt and we charge on the value of loans getting disbursed using the platform. So it's a pure fee income. No risk on our balance sheet.

The placement business is all fee incomes without taking risk on the balance sheet. Essentially, there are very few companies who can monetize their strengths and assets and given we are a high-impact credit business, we are beginning to do that.

Sushil Choksey: Have you attached on the same platform anything to do with LAP loans, MSME loans or anything else?

Ashish Mehrotra: We can do all of those products Sushil ji. We do originate LAP. We do gold. So if the bank wants any of those asset classes or any other lender wants those asset classes, we can seamlessly connect APIs and flow. And it is very agile. So you can decide to select that one only want people living in certain geographies, certain income, certain categories and you can change that every three hours. That's the agility of that platform.

Sushil Choksey: How many banks do you expect to do tie-up for?

Ashish Mehrotra: Sorry, sir?

Sushil Choksey: Right now, you said you have two private sector banks from South Indian, one PSU bank. How many more banks will you tie-up for?

Ashish Mehrotra: We have one. Hopefully, we go in line with the public sector banks and then others we continue to expand as we go about doing it, sir.

Sushil Choksey: Is this platform directly competing with Yubi or is it something different?

Ashish Mehrotra: I think there are platform providers and there are platforms who have 5 years of demonstrated results. I have underwritten 25 million, 30 million loans on this platform and this platform for us has gone through every change in regulation, every way that we account we accrue. So I don't think there is anyone who has a platform as robust as this. Obviously, yes, we do compete with them, but there is a tested platform.

Sushil Choksey: Do you charge anything for the platform?

Ashish Mehrotra: We have 400 partners on this platform. So I can, unlike the other tech businesses we already have partners on this platform. The original investors can come and connect.

Sushil Choksey: Do you charge anything for the platform or it's only a fee collection on the product generator?

Ashish Mehrotra: No, it is essentially for a fee business depending on how these loans work with the investors.

Sushil Choksey: By any design or product, you can do insurance or any other financial products on this platform via design?

Ashish Mehrotra: Not just those capabilities, sir. The platform has the capability to offer embedded platforms, we added some of that, but largely these are offered by the originators and not by the investors. So we can, it's a pretty agile platform for us to adjust to.

Sushil Choksey: And this housing finance company, whatever the way it is outstanding you don't want to speak on numbers, but can you tell us that what is the percentage of loan which is outstanding have you provided for specifically to that account. So we know that risk is only amount of that much outstanding, rather we don't want - I'm not taking names, so you may say 25, 50, whatever percentage is?

Ashish Mehrotra: So Sushil ji one we don't provide specific comment at an obligor level. But unlike the conventional term loan lenders, our approach is loan to originate. So we have a specific charge on a specific portfolio which is broadly assigned to us. And what we believe could potentially be beyond the fair market value we would have provided over 65% of the residual book value.

Sushil Choksey: And the separately provided portfolio too which is only assigned to you, how much is performing portfolio in that?

Ashish Mehrotra: That's already beginning, that's already get built into the fair market value, Sushil ji. I don't think I'll be able to answer beyond this because I can’t discuss specific strategies at an obligate level. All I can say, I may be steps ahead, I may be many steps ahead of any other lender.

Sushil Choksey: Can I assume you're fairly ahead of the curve which is required?

Ashish Mehrotra: I think we are ahead of the curve, but we still have to go through the process as it goes through. We are ahead of the curve, but there is obviously NCLT and other processes we have to deal with, but we are pretty prudent and we are very cautious and the action we have taken.

Sushil Choksey: Can I assume that your borrowing costs has peaked?

Ashish Mehrotra: I think so. We did see a little bit of change in the quarter because of the way the liquidity costs, but I see as I look forward, I see a borrowing cost providing incremental relief for the spread expansion. We've also been pretty judicious, so I think we are ahead of the curve even of that. If you compare us to our peers with a similar rating curve and we will stay ahead on that.

Sushil Choksey: Good luck to the team and thank you for answering all my questions.

Moderator: Thank you, sir.

Moderator: Thank you. The next question is from the line of Purshotam from Volkswagen. Please go ahead.

Purshotam: Hi, sir. Thank you for giving me the opportunity. So my first question is as sir mentioned in the commentary as well the next two quarters will be a bit cautious for us. So what will be the guidance for financial year 2025-2026, growth guidance?

Ashish Mehrotra: I think we will, like I said, we will remain cautiously optimistic in meeting the quality of the business. So the idea is to chase the quality growth and we're just not chasing at it. We're fully cognizant of the current challenges in the environment. I think we should end somewhere, between 15% to 20% growth on an annualised basis. So that's where it should be.

Purshotam: Okay. Thank you, sir. And my second question is, what is the dividend policy of Northern Arc?

Ashish Mehrotra: I think that's a debate in our board. It's one of the important agenda items we've been fully cognizant and this is an entity we need to work on it. We're working this through and hopefully should be able to come back to you guys before the next call.

Purshotam: Okay. Thank you.

Moderator: Thank you. The next question is from the line of Balaji Kasal from Profocus Value. Please go ahead.

Balaji Kasal: Yes. Good evening, sir. I have only one question regarding MFI. As you see the data, you are downsizing it. Also, the CFO mentioned you're monitoring the credit side of portfolio. I just want to know what is the plan in the near future? Will you downsize to zero or close down or sell off it subject to MFI or you want to be or remain the player there?

Ashish Mehrotra: Thank you. I think a very interesting question. Like I said earlier we are a diversified lending business. We focus on customer segments. We also have an ability to dial up and dial down depending on opportunities and challenges. If you see our numbers closely, you will see there is a big growth in the MSME space, in the consumer lending space. MFI, we've been cautiously bringing it down over the last three, four quarters.

If you look at over the last 3 years, the numbers are very different. And we will build back with our scorecards as we find the market stabilizers and the regulation and market stabilizing over a couple of quarters. It's a very interesting business. We stay deeply committed to ensuring the flow of credit to the underserved individuals.

As both the regulatory, self-regulatory bodies in the MFI sector, Sa-Dhan and MFIN we are working very closely with them. And I think as things begin to stabilize, we will continue to work and stay committed, but I think our strategy to answer your question very specifically is to ensure no sector barring MSME can be more than 30% of our balance sheet. MSME, we can go up to 45, 50%, which includes large portion of the secured lending.

So sectorally, we remain diversified because over the last 15 years, we've seen the businesses and customer segments tends to face challenge and for you to be a resilient and a consistent performer, you need to ensure that you are able to manage the risk more proactively. And that's been our approach and reflects in our track record for over a decade and a half.

Balaji Kasal: Thank you. All the best to the team.

Moderator: Thank you. The next question is from the line of Chintan Shah from ICICI Securities. Please go ahead.

Chintan Shah: Yes. Thank you for the opportunity. So sir, firstly, on the leverage piece so now post the IPO, our debt-to-equity is now 2.8x roughly. So what is the level up to which we can again scale our debt-to-equity firstly on that?

Atul Tibrewal: So Chintan, we are currently at around 2.5. The rating agencies, the regulators, the lenders, they all are comfortable anywhere between 4 to 4.2 times. So this will give us enough headroom to grow our balance sheet for the next 2 years, 2.5 years. So we will not be required to raise any equity if we continue to grow at a CAGR of say close to 25% to 30% for the next 2 years and 2.5 years at least. So the next raise should happen in FY28.

Chintan Shah: Sure. And ROI is probably – sorry.

Atul Tibrewal: We were having around INR80 crores to INR90 crores of profit every quarter. So that will also give us enough headroom and we have raised around INR980 crores this year.

Chintan Shah: Sure. I was just trying to understand from the ROE perspective. So given how far can the ROE go considering a probably ROA of 3% to 3.5 percentage so what would be the ROE number, I was looking at that number and secondly sir on the placement volume, the placement volume seems to be flat on a nine month basis, but there seems to be a dip in the fee income from INR20 crores to INR17 crores. So any change in the take rates here or how should we read this?

Ashish Mehrotra: I think it's a function of the credit. This business is a function of credit offtake and not only us and I'm sure most of the people before us in the comments we would have given to you, they've been cautious and that's one of the reasons. But I can also tell you it also provides an opportunity for us to provide more structured and credit solutions to the institutions as liquidity becomes tighter. I think that we are pretty bullish.

And not only this is an important quarter for that business, but also as we go forward among the product heft we have, that will continue to be a meaningful contributor to our business as we go forward there. We've actually did a very interesting transaction when the consumer finance sector weightage went down and people were struggling to raise money.

So we've had done very interesting transactions by moving thousands of crores of money in a manner which provided great solutions to lots of people. So we continue to stay committed. I think this business, as the credit demand increases it is a massive demand, but as the credit demand increases, we'll see an increase in this line.

Chintan Shah: Sure. And also on the MFI fees also what is the write-off policy for the microfinance business currently?

Ashish Mehrotra: Our policy is we write off all unsecured loans at 90 DPD

Chintan Shah: Sure, 90 plus DPD. And so on the Stage 3, which is currently INR110 crores, that's the data-keeping question. Could you help us with the breakup of the Stage 3 into the segmental, a segmental breakup for Stage 3 and on Stage 2 as well, if possible?

Pardhasaradhi Rallabandi: Out of the 110 crores of Stage 3 exposure that we have spoken about, the large pieces are in affordable housing around INR25 crores and MSME LAP was around INR39 crores. And there is obviously microfinance business we do not have much because of the write-off policy. And there are certain mid-market exposures, but the large numbers are MSME LAP.

Ashish Mehrotra: If you look at it on a year-to-date basis, it's fair to say between the consumer finance and the MSME are the two large constituents. MSME are the two largest constituents of full correct credit cost.

Chintan Shah: Sure. And also on the collection efficiency, particularly for the microfinance piece, even if we exclude Karnataka, so could you give just some broad sense on how the trend has been so far? We have seen for most of the lenders, the collection efficiency have improved from November to December, and they have also sustained kind of in January? So how has been - I think we mentioned the collection efficiency was better in December, but how has been the trend in January and February so far also if you could share some thoughts there?

Pardha Yes, collection efficiency has improved between November and December. January was flat or slightly lower. February is a little too early. The collection cycle is still last till 7th and 8th of the month. And then there are collections after that on a daily basis. So to the next thing, for February it is a bit early to comment on, but between December and January, the collection efficiency remained slightly lower.

Ashish Mehrotra: Chintan, the way we look at it, one is the dot, two is the line, three is the trajectory. We audit the trajectory before we formally comment on the improvements.

Chintan Shah: Sure. And sir, just one last question. On the interest reversal part which you mentioned in the commentary, so that was specifically for MFI and so that was towards the account which we have written off for the quarter?

Atul Tibrewal: No, Chintan, it was for all our loans which have been written off and also which were in Stage 3. So it was for all the portfolios, not specific to MFI and the amount was INR24 crores.

Chintan Shah: INR24, sure. Okay, that's it from my side. Thank you and all the best.

Moderator: Thank you. Ladies and gentlemen, we will take that as our last question for today. I would now like to hand the conference over to the management for closing comments. Over to you, sir.

Ashish Mehrotra: Thank you very much. Thank you for joining us today. I wish you all a happy Valentine's Day. Thank you and have a great week. Thank you.

Moderator: Thank you. On behalf of ICICI Securities Limited, that concludes this conference. Thank you all for joining us. You may now disconnect your lines.