



“Northern Arc Capital Limited
Q1 FY26 Earnings Conference Call”
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MODERATOR: **MR. CHINTAN SHAH – ICICI SECURITIES**

Moderator:

Ladies and gentlemen, good day and welcome to Northern Arc Capital Q1 FY26 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 the conference call, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Chintan Shah. Thank you and over to you, sir.

Chintan Shah:

Thank you, Viren. Good evening, everyone, and welcome to the Q1 FY26 earnings conference call for Northern Arc. We have with us from the management; Mr. Ashish Mehrotra, MD and CEO; Mr. Atul Tibrewal, CFO; Mr. Pardhasaradhi Rallabandi, Chief Group Risk Officer and Governance Head, and Mr. Chetan Parmar, Head Investor Relations.

I would like to thank Northern Arc Management for giving us the opportunity to host this call and congratulate them for a good set of numbers. So now, without further ado, I would now like to hand the floor over to the management. Thank you and over to you, Ashish, sir.

Ashish Mehrotra:

Thank you very much, Chintan. I appreciate your kind words. Good evening, everyone. I am delighted to welcome you in today's call. Thank you for joining us for today's conference call to discuss Northern Arc Capital's performance for the quarter ending June 30, 2025.

I am also joined in this call by my colleagues; Atul Tibrewal, our CFO, Pardhasaradhi Rallabandi, our Group Risk Officer and Head of Governance; Chetan Parmar, Head of Investor Relations and Jigar Seta, Head of Strategy.

As we step into 2026, it is important to acknowledge that we are coming off rather an eventful fiscal year, i.e., FY25, which was marked by several headwinds, including a decline in credit growth, stress in the microfinance segment, delay in rate transmission, regulatory shift in MFI and digital lending space, global macroeconomic volatility and these sector created significant challenges across the lending landscape.

However, as we enter into FY26, we are beginning to see some early signs of recovery. We witnessed two rounds of rate cut from the regulator, offering much needed relief, both in terms of pricing and liquidity. The macro indicators are turning positive; rising consumption demand, increase in fixed capital investments by large corporates, which we believe will expect to flow downstream to MSMEs, strong agricultural prospects supported by above normal monsoon forecast and continued capital push by the government.

All this abodes well for the economy and sets a positive growth momentum for the year ahead. Having said that, we do expect the residual impact of FY26 stress to linger through the first half of the year, but as we approach the festival season, we anticipate the credit environment to stabilize, allowing the industry to regroup, reallocate resources efficiently.

Further amplifying this, in the RBI's recent rate cut combined with reduction in the risk weight for bank lending to NBFC, this sends a clear constructive signal reinforcing the regulator's intent to support credit flow, easing liquidity constraints and promote sustainable growth.

As we begin FY26, our aim is to carry forward the lessons we have learned from the last year's headwinds and ride the regulatory tailwinds to build a more resilient, responsible and high-performance business.

Let me now turn and talk more about Q1FY26 performance. I am pleased to share that we recorded the highest ever quarter 1 placement volume in Northern Arc history. This serves as a strong indicator of revival of credit demand that we have been anticipating.

Traditionally, Q1 is seasonally a soft quarter for credit uptake. This year, performance was further impacted by the residual impact from FY25, leading to the cautious deployment of growth and ongoing geopolitical headwinds continued to weigh on the sentiments. As a result, overall credit growth remained muted at about 12% on a YoY basis.

Growth was predominantly led by our MSME business, which has been a strategic posture. Our AUM in the MSME business grew by about 34% YoY. This was followed by growth in the consumer finance segment, which grew by 25% YoY. And our intermediate retail, which is more a credit solution business, grew by about 12% YoY. However, if we exclude the growth in the rural finance business, the overall growth of Northern Arc would be 20% YoY.

In the rural finance segment, we are seeing meaningful improvement. The PAR 0+ accretion has reverted to March 24 level at 0.5%, primarily driven by the broader recoveries across most of the geographies, excluding Karnataka. While in Karnataka, as we started showing early signs of stabilization, we believe there is still a significant headroom for further improvement, and we are actively working towards that.

Our fee franchise, which is a unique fee franchise, saw strong traction as well. With the recorded placement volume and consistent accretion in our funds business, our core-fee income coming from our placement and the fund management grew by about 24% on a YoY basis, while the balance sheet grew by about 12%. This reinforces our strategic posture of building a credit solution ecosystem, not just pure balance sheet-led model.

Our Credit quality continues to be best in class, driven by proactive risk management and conservative provisioning policy. We continue to maintain a high-quality book, prudently provide for stressed assets and unsecured exposures.

Having said that, the credit cost remains elevated during the quarter due to the tail impact of FY25 stress. However, we believe the initiatives being undertaken across should help us going forward, i.e., essentially driven by responsible and sustainable lending and implementation of MFIN guard rails. We have ensured that all the assets under the rural finance are now under CGFMU guarantee scheme and strengthening our collection infrastructure. This will help stabilize delinquencies going forward.

Given the improvement in the environment, we expect H2 credit cost to land somewhere between 2.7% to 2.9%. On liquidity and capital, our liquidity and the funding remain well capitalized. Atul will talk about it, and I don't want to steal his thunder, but fair to say we are top quartile among our peers in managing our liability franchise. But good to dwell for couple of minutes as we look at strategies and way forward.

Given the strong foundation and the growth over the next three years, as we continue to execute our strategy, we are well positioned to achieve an AUM growth target of 20% to 25% annually. Essentially driven by big growth in the direct-to-customer business, taking our mix to 70% by FY28, which will be predominantly led by lending to MSME, consumer and rural finance.

We will continue to judiciously expand our intermediate retail business to build a unique and a very powerful fee franchise, which will help us gain incremental 30 to 40 basis point on RoA, which essentially reflects in the loaded NIM.

Our credit conscious approach will help us reduce and ensure that the credit cost on a year-on-year basis remains well within the desired range. Coming to operating efficiency we continue to capitalize and leverage on our current capabilities to get better expansion in our net interest margin and opex ratio is expected to remain within the range of 3.6% to 3.9%. With solid execution, we expect the ROA to get to 3.7% to 4% with ample growth headroom for next 3 years. We are confident of delivering ROE in the range of 16% to 18% over the next three years.

We are excited about the journey ahead and are confident in our ability to execute, capitalize on emerging opportunities and stay ahead with the principles of sustainable and inclusive growth. With that, I will now hand over the call to Atul to walk you through Q1 numbers in detail.

Atul Tibrewal:

Thank you Ashish and good evening everyone. I appreciate you joining us for Northern Arc's Q1 FY26 earnings call. Let me walk you through the financial performance. Our assets under management stood at INR13,351 crores, reflecting a growth of 12% year-on-year. Within the AUM mix, the direct-to-customer business contributed 53% with MSME finance at 20%, consumer finance at 26% and MFI Consciously calibrated at 7%.

Net interest income for Q1 FY26 stood at INR 298 crores, which is up 10% Y-o-Y. Net revenue including the fee income, rose 9% Y-o-Y to INR325 crores. Fee and other income grew by 8% Y-o-Y to INR 27 crores, driven by robust placement volumes during the quarter. Our cost of funds for Q1 FY26 was 8.9% compared to 9.3% in Q1 FY25. Incremental cost of funds for the quarters stood at 8.7% vs. 9.3% in Q1 FY25, which is an improvement of close to 60 basis points.

Operating efficiency also improved our opex ratio by 57 basis points Y-o-Y to 3.5%, aided by tighter cost control. As a result, our pre-provisioning operating profit rose 18% Y-o-Y to INR207 crores, compared to INR175 crores in Q1 FY25. Provisions for the quarters were INR102 crores, largely due to stress in the MFI segment. We believe this stress has peaked and should moderate going forward.

On a percentage basis, the overall credit cost for Q1 FY26 stood at 3%. Asset quality remained stable with GNPA at 1.1% and NNPA at 0.6%. Profit after tax for Q1 FY26 stood at INR 81 crores, compared to INR 93 crores in Q1 FY25 and INR 38 crores in Q4 FY25.

On the liabilities front, in line with our debt strategy and AUM growth plans, we have continued to diversify our funding base, with a very clear focus on long-term sources. Liquidity remains quite comfortable, with positive cumulative mismatches across all the time buckets. As of June

30, 2025, we held surplus liquidity of around INR600 crores and undrawn sanctions of over INR1,200 crores from various banks and institutions.

Total borrowings at quarter end was INR9,422 crores, with approximately 75% linked to variable interest rate, positioning us well to benefit from the decline in interest rate scenario. Our funding mix remains quite diversified, 30% from offshore and DFI sources, and 70% from domestic banks, institutions, and capital market. Tangible net worth stood at INR3,532 crores, up 27% Y-o-Y.

We have strengthened the balance sheet materially. Our debt-to-equity ratio improved from 3.9X in March 24, to 2.7X as of June 2025. Capital adequacy remains quite strong at 25.5%, well above the regulatory requirements, giving us ample headroom to grow the balance sheet over the next 3 years. Thank you so much.

With this, I would like to open the floor for questions.

Moderator: Thank you. We will now begin the question-and-answer session. We have our first question from the line of Digant Haria from GreenEdge Wealth. Please go ahead.

Digant Haria: Yes, hi. Thank you for the opportunity and congratulations on the really good performance of the Intermediate Credit and the Consumer Finance Division. My first question is on provisions. This quarter also we had INR19 crores because of the DLG provision. So, is it safe to say that INR80 crores-INR85 crores of provisioning we have peaked at this number and going ahead every quarter, we will see some bit of decline?

Ashish Mehrotra: We have done 100% provisioning on account of DLG. There is no more residual stuff. Whatever you will see, you will see the core provisioning. Anyway, our provisioning tends to be prudent on Stage 1, Stage 2.

Digant Haria: Okay. So actually, it would be safe to assume that INR80 crores is probably the number, right, the peak number and as microfinance improves, we may improve from here.

Ashish Mehrotra: As I said earlier, our PAR 0+ accretion has reached 0.5%, which was there in last year's beginning, which is March 24, it tells you that broad stabilisation has happened. I said Karnataka will still see a couple of more months.

So there is further scope for improvement is the right word to use. I think we are in a good position and fairly confident to manage if there is residual stuff as we move forward. And we have been very cautious in our own approach dealing with this entire thing.

Digant Haria: Right Thanks. My second question is on the capital allocation at Northern Arc. Like, as an external observer, if I see the intermediate credit and the consumer lending, they take very little offtake and they deliver very good ROAs, ROEs for business. But when it comes to retail, it has been like 4 years now, probably takes the largest portion of the operating expenses and capital employed. If I just do a simple sum of the parts, I think that our retail business is not even making a 0% ROA.

So my question is, you said that in the long-term, we would want to increase the rural business, the MSME business. So, like, what have our learnings been of the last 4 years and why do we want to, because this business has not given us any meaningful return over the last 2, 3 years, why are we doubling down on that? And -- yes, so that's the first question on this capital allocation.

Ashish Mehrotra:

Let me try and break this into smaller parts. We as management and at a Board level are very sharply focused at the segmental product profitability. That's the way we conduct our business. We allocate capital, depending on where will we make both the strategic investments and where will we get the expected hurdles for return on assets.

Let's use return on assets and return on equity for this chain. We also know the headroom for the expansion on the return of assets as we build the business forward. Our retail business including Retail Partnership Based Lending today is extremely profitable. If I look at whether it is digital lending business, which over the past few years, has made fairly good return on assets, significantly better than what we have on an aggregate basis.

Credit solution business is a very unique business, and we are building more on expansion in our capability to do a lot more credit solution. Fair to say we are very uniquely positioned, our ability to originate large amount of retail credit, our ability to process large quantum of retail credit, our ability to run heavy technology for the credit to flow from originators to investors, our ability to sell that credit to institutional investors, we have demonstrated that for last 15 years.

Our ability to sell that to the retail investors through our bonds platform, our ability to invest in that credit from our fund management business, if the fund has the right set of thematic opportunity for investments, our ability to support it from a balance sheet and our ability to manage and collect.

I think that's a very powerful business and that business for us generates more than 3 plus return on assets is a function of how strong the fee franchise runs and that's why, what we said on a forward looking basis, as you combine all of these pieces, we will get to where we want to get to. Obviously, we dealt with the situation in the rural finance business, which is cyclical in nature, where we saw what the issues were, we were very proactive in bringing down our exposure and managing that risk.

We've also now introduced, our own scorecards to where we see what kind of outcomes will we get in case such one in 10-year risk events occur and I think we are pretty confident building it as we build forward, but we will be cautious and as we go about doing it.

Digant Haria:

So, specifically, Ashish, the question was more for these two pieces of our business, the direct-to-consumer, LAP business and the microfinance business, because I think the microfinance has obviously given us a lot of pain. So, between the two, how do we take it forward and are we thinking of any move...

Ashish Mehrotra:

On a forward-looking basis to what I've said, both -- all these businesses, whether it's consumer lending, whether it's MSME lending, whether it's rural finance, they will eventually be all in the

range of 3.7% - 4% RoA, if not better, ideally better, than what we've said as an outlook to the business, and there, barring the rural finance, at a product level none of them are negative today.

And we do hard cost allocation through going down to direct costs, support costs, management costs. So, we take a very hard look when we look at allocation of our resources and capital.

Digant Haria: Okay. Okay. I hope we see those divisions also delivering, because it's taken a lot of capital and opex. So, all the best for that, Ashish.

Moderator: The next question is from on the line of Adarsh Parasrampur.

Adarsh: Hi, Ashish and team. Congrats on good numbers.

Ashish Mehrotra: Hi.

Adarsh: Question on SME and consumer finance in context of one, some commentaries coming from peers on some problems on SME that they're facing, little more to do with small-ticket SME, so qualitative comments on that side. And on consumer finance, last 12 months, 18 months where little disruptive models changed, DLG came in, then there are some withdrawals happening as well. So, just wanted to understand, is things stabilized now? What is your outlook on these asset-quality comments on these two businesses?

Ashish Mehrotra: Okay. So, I will give you response not specifically to our balance sheet but also given that we moved a sizable amount of assets for securitization and given the multiple relationships with Intermediate Retail Partners. So, I'll take a broader industry view as we talk about it. If you actually look at it, in the consumer finance space, three things have happened over the period of last two years.

One, the shift away from the small-ticket personal loan, buy now, pay later, its mix in the consumer finance space has come down. The second is the short-term high APR loans given the RBI intervention last time on transparency and pricing. That's mix at an industry level we've seen the reduction. And third is more prudent given the consumer finance business or the personal loan business saw a little bit of higher elevated credit costs.

But as we look at it, it's broadly stabilized today. As long as you're able to price for risk, I think we're able to get the right set of outcomes. In our own business, we price for it through leveraging both the FLDG and the pricing mechanism to ensure we're targeting the right set of customer cohorts, which will give us a decent risk-adjusted yield of about 15% to 17%. I think that's the one part.

In the unsecured SME loans, we are seeing higher elevated flow rate as a consequence of that higher credit costs. And I think there is some amount of tightening which we have seen our peers doing it. In our case, we don't have a high concentration of unsecured business loans in our balance sheet, so we are protected in that way.

But on consumer, I think, we've seen stabilization, because you're also targeting a better set of customers. When you were lending at 30% and you're lending at a short-term, you had a very

different target customer profile. And as you start lending for longer term, you're targeting a better salary profile.

So, I think we've seen stabilization in consumer finance. Unsecured business loans go through the cycle. There is a period. We've seen that across industry. But I think part of that spillover of that effect coming from MFI should also get washed out by this quarter. I mean, by H2, you should start seeing improvement in those numbers.

Adarsh: And the other question is slide number 34 on the ROA tree walk. Our margins moved from 10% to 8.9%. Yields were down 80bps - 90bps Q-o-Q. Part of it may be a reduction in the MFI book, but I just wanted to understand because that's the consumer book...

Ashish Mehrotra: You picked it up right. Two things. One is the reduction in the MFI book. You saw what this book was. It's now down and we are rebuilding this book. And the second is we've consciously exited last year some of the consumer segments what I alluded to earlier.

So as a consequence, as we rebalance the book, our NIMs will come back to where they were and they'll continue to expand with the change in the mix with our direct-to-customer book inching quarter and quarter towards 70% what the targeted our aim is.

Adarsh: Perfect. My last question, Ashish, is on credit cost. We are at 3% with some one-offs on DLG. You did mention some time between 2.7% to 2.9%. Is that the exit credit cost or the average that you expect for the year?

Ashish Mehrotra: I think our outlook is that we've seen the elevated part of the residual impact from FY25 coming into this Q1. I think by end of the year we should be able to end on an aggregate basis credit cost of below 3%, anywhere between 2.8% to 2.9%. I think that's the outlook we will work towards. We're working very sharply to ensure our target client model remains true to get the right set of outcomes.

Adarsh: Perfect decision, team. Thanks for answering the question.

Ashish Mehrotra: Thank you.

Moderator: Thank you. The next question is from the line of Avinash Singh from Emkay Global Financial Services. Please go ahead.

Avinash Singh: Yes, good evening. Thanks for the opportunity. Again, continuing on the asset quality and credit cost outlook. So broadly, if we were to sort of, hear the commentaries from various lenders, I mean, there has been concerns around, of course, MFI likely bottoming out, MSME unsecured piece, particularly some concerns, I mean, increased concerns.

Additionally, if we look at the CV segment, I mean, used and new both is where there is kind of some players thinking of increasing stress and all. In your scheme of things, of course, that vehicle piece is relatively smaller, but that was also intermediated.

But from whatever you are gathering, because, of course, you will be seeing what kind of a trend you are seeing as far as the stress buildup is concerned in the vehicle segment? So that's question one.

And second, I mean, when you are sort of a kind of a hint, I mean, giving this guidance that credit cost for the year should improve from here onwards, which are the segment, I mean, that is giving you sort of more-and-more confidence that, I mean, you will be able to kind of do better from here. Because, I mean, if we look at different players, there is noise around most of the segments where you are? These are my two questions. Thanks.

Ashish Mehrotra:

Hey, Avinash, very insightful as you've connected all the dots given some of the early conversations you would have had with the peers. And I think it's fair to say, MFI is a good leading indicator to how credit is being performing.

It's also very different operating model, but it's more group than JLG in today's context if one just steps aside and reflects on it. And you've seen as the over-leveraging happened there, you saw impact of that flowing into unsecured personal loans, unsecured business loans, and so on, so forth.

You've seen some of the results where it then transcended into small businesses, into commercial vehicles, and so on, so forth. Our sense is, as the new guardrails come into play, and to what I said, that we've seen an improvement in PAR 0+ accretion, this means the flow rates, the forward flow has significantly reduced and we are broadly in line to where we were in early 2024. That means we should start seeing some amount of improvement, not only in MFI, but also across as it flows forward.

Further to protect, we've done two things. We've also recalibrated our scorecards for our own piece because we've been doing that to ensure that we get better set of outcomes. It might have resulted in a reduction in the approval rates, but that's, I think, fair to do during this time because you want to build a better quality, high annuity income.

And the second, we've also taken CGFMU cover incrementally for all MFI assets coming on board from March onward. So, I think overall, as we see improvement in the PAR 0+ accretion in MFI, we'll see part of that impact flowing into some of the other unsecured pieces over the next 2-3 quarters.

And MFI is actually the first one to call out in that segment that there is a trouble. If you're a monoline, if you're a single product pony and you're having a challenge in that product, you have no choice but to highlight that there is a challenge you're dealing with. I think that's my take. That's what we are seeing.

Avinash Singh:

Okay. Thank you.

Moderator:

Thank you. The next question is from the line of Deepak Gupta from JM Financial MF. Please go ahead.

Deepak Gupta:

Hi. Good evening, team. My first question was on the credit cost guidance. I just wanted to understand it a bit better. Given the fact that you reported 3% credit cost for the first quarter and you're guiding that at the end of the year you'll be at 2.8% to 2.9% despite the fact that this quarter had DLG which may not be there in the coming quarters, are we expecting credit costs to go up in the next few quarters? Is that what the guidance is?

Ashish Mehrotra:

No. I will ask Pardhasaradhi, our Chief Group Risk Officer, to talk about it in detail?

Pardhasaradhi R.:

No, not really. The way to look at it is whatever credit stress is there in the system continuing from FY '25 is something that should play out by September quarter in H1 of this year and H2 should be reasonably better.

And in line with what we have been doing all this while we have been reasonably conservative and building up the provision base that we have both for good book and for stressed assets and the balance sheet.

With reasonable amount of conservatism we are talking about 2.7% to 2.9% being the full year credit cost, but having said that, it's not that we are expecting more stress or higher or elevated stress than this, than what we have seen in '25, in '26, that's not the case.

Obviously there will be balance sheet growth and there are certain segments of the business where we would plan for higher credit cost, the growth can happen in those segments because of which we might see the ultimate credit cost landing between 2.7% to 2.9%, but if you look at it, I think stress on the portfolio is the residual of FY25 that we are carrying in H1, we are continuing, but we don't really think that the '26 on an average would be higher stressful than what we have seen in Q1 and what we have seen in '25. But having said that, it's good to be a little cautious, a little conservative and guidance is something that we should be reasonably conservative about.

Deepak Gupta:

Okay, the question was stemming from the fact that your Stage 2 and Stage 3 loans are showing 50 basis increase, so I was just wondering that you are expecting further slippages to happen from Stage 1 to 2 or 3 in the coming quarters?

Pardhasaradhi R.:

Obviously, Stage 3 is not really an issue because that's already in PAR 90 and we have provided adequately as per the policy and there is a Stage 2 increment of 1.8% to 2.1% which is pretty much in line with where we should reasonably expect the numbers to be in this environment. 96.7% of assets is in Stage 1 bucket. Combined Stage 1 and 2 assets of 98.8% is a comfortable position to be in.

Deepak Gupta:

Sure. And my second and last question is when you are looking, when you are targeting a return on asset of 3.7% to 4% in the next three years, what kind of credit costs are you envisaging and in terms of what kind of NIMs are you looking at given the fact that microfinance is under due risk, but do you plan to continue with that segment in the coming quarters and years?

Pardhasaradhi R.:

Three years is obviously a long time, and we should budget for cycles, etcetera. The way to look at it is the way we plan our business mix, we would plan for the credit costs to be contained in the range between 2.5 to 3 and that with the expansion of the NIM and the leverage going up

and obviously we have scope for balance sheet growth at the current capital level. With all this put together, we should have a reasonable ROA level, return on asset level and return on equity levels.

Moderator: The next question is from the line of Prateek Sen from Dexter Capital Advisors.

Prateek Sen: What is the channel of sourcing of our loans for D2C book? How much is it from our own branches and from the partners? Can you hear me?

Ashish Mehrotra: Yes. If you look at the D2C and split it into two parts, one is the digital sourcing, second is the branch-based sourcing. Branch-based sourcing is 100% between MFI and secured MSME lending is directly through a branch network, total 360 plus branches to originate. Digital lending happens through our digital partners, and we probably run the most sophisticated high-quality lending platform. We spoke about it multiple times. On that platform, we underwrite anywhere between 18,000 to 20,000 loans a day. It is a very customer-centric, product-agnostic platform. That's how the split is.

Prateek Sen: What is the blended yield on this loan and how is it shared with the partners?

Ashish Mehrotra: We said in consumer finance, we make a risk-adjusted yield of anywhere between 15% to 17%. On our secured SME lending business, we make a yield of about 18.0% to 19.0%. On our rural finance book, which is pretty low, we make about 24%.

Prateek Sen: All those partnerships have FLDG in place, right?

Ashish Mehrotra: Yes, all partnerships have FLDG construct.

Prateek Sen: Understood. On the monetization of our tech stack and platforms, Nimbus, nPOS, Nu Score, what is the yearly revenue that you are collecting from these, if you can share that?

Ashish Mehrotra: We are seeing early traction. We are now live with two institutions in the nPOS. We are working with one large non-bank finance company and three other banks to take live. We demonstrated in banks we are live with to do across products from an SME loan to a secured gold loan. Nobody has the capability to do so many products through a single platform. Scorecards are now being used by two or three institutions. We are expanding that.

That's why when I spoke about credit solutions as a unique business, there are very few businesses which have full capability to originate across the retail assets and the retail lending platform to do all what is required to be done. One is to originate large quantum of credit between our 350 plus NBFCs whom we work with to take that retail credit to underwrite the risk of that retail credit, place that risk and process that through our own technology platform which is Nimbus, make it available to institutional investors.

90% percent of people who invest in these assets have been buying these assets from us for over three years. To make that available to retail investors through our own bonds platform called Altifi.ai, please do download the app and use it. It is a good way to allocate some of your wealth into high-yield bonds.

Then is to take it and invest from a funds business which is done really well. We run 12 funds so far. Six of them have closed. The average gross yield over the 9 years on the performing credit is about 14%, then supported from balance sheet and service across the asset classes. So, I think that is a unique capability we have built, and we continue to expand, fee franchise, leveraging all of that to support what we do.

More importantly, it gives us access to an ordinate amount of information and ensures that we Northern Arc become a great learning organization as we see the flow of all of these loans and the performances of these loans. So, we have over 45 million time series of loan performance data. So, we broadly look at it differently.

Prateek Sen: Understood. A follow-up question on the yield. Is the blended yield figure same as the average borrowing rate for the borrower or is it the numbers you quoted, is it post commission?

Ashish Mehrotra: Atul, you may have to take that.

Atul Tibrewal: The yield that we show as part of our investor deck is the one that we charge to the end borrower net of the fees that we pay to our partners. So for the other businesses, it is the interest that we charge directly to the end customer, but for the digital lending business, which is largely the consumer business, it is the net yield adjusted with the services fees.

Prateek Sen: Okay. Understood. Thank you. Thank you.

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

Pawan: Thank you for the opportunity. So, my question is mainly on the personal loans. The quarter-on-quarter growth in personal loans is down to 3.3%. Is it more of a seasonal aspect or more related to calibration of score cards you mentioned? And on the corollary, how will the growth rates look going forward? Related to this, earlier you mentioned that you are moving higher in the credit quality in personal loans. So, what will happen to the yields in this segment? Hello, could you hear me? I think you are audible.

Ashish Mehrotra: I spoke about it earlier. Yes, we did moderate some part of consumer. That is essentially on three things. One is sensitivity in line with the fair lending code. The second is consciously exiting the short-term personal loan, which we all saw the issues it was creating. The third part was also building towards a better quality customer cohort, which is a longer term rather than running on a treadmill. I think those three were very conscious decisions we made.

We believe that the yield, what you see in compression, is largely led by the reduction in rural finance as a mix of our overall business. And as we recalibrate the business, we believe the yield will come back quarter-on-quarter to where we were. And actually, as the mix improves on a quarter-on-quarter basis towards retail, you will see expansion in the yield and in the NIM.

Pawan: And how will the growth rate...

Ashish Mehrotra: Growth is about 25% YoY, just to correct on the consumer finance. If you refer to the slide 13, you will see that quarter four tends to be a better quarter.

Pawan: Sir, any guidance on the growth rates going forward for personal loans and the MSME?

Ashish Mehrotra: We said broadly in line with the overall guidance we've given. And we've also said specifically how we want to play in these three segments, which is MSME, consumer and rural.

Pawan: Sure. Thanks.

Ashish Mehrotra: Thank you all.

Moderator: Thank you. The next question is from the line of Abbas Varma from East Green Advisors. Please go ahead.

Abbas Varma: I have a question on your branch network strategy. So, in one of your earlier calls, you had mentioned that branch expansion...

Ashish Mehrotra: Hello, we can't hear. Hello?

Moderator: As the participant has left the queue. I would like to take the next question from Chintan Shah. Please go ahead, sir.

Chintan Shah: Thank you for the opportunity. So, sir, just one thing on our incremental cost of funds. So, I think incremental cost of funds have seen quite a sharp decline to 8.7% versus 9.3% Q-o-Q. And this is almost equal now to FY '22 level.

And also, I think liquidity has quite inched up, improved in this quarter. So, as such means what changes, I understand that it could be partly due to reparate, but so what kind of cost of borrowing could we expect? And could you just throw some more light on the cost of funds and the liquidity front?

Ashish Mehrotra: My colleague Atul will answer this question.

Atul Tibrewal: Thanks, Ashish. So, Chintan, as you know, the incremental cost of funds has come down definitely but what we actually now need to do is to bring down the overall cost of my book. The good thing is that 75% is variable. And unfortunately, the repo rate transmission has not yet started happening by the banks.

But definitely this is something that we will now see. And on the book cost of funds, which is currently at 8.9%, though that has come down from 9% level, that should come down even further as we get more and more benefit of the MCLR cuts by the banks.

Secondly, around 25% of the book is linked to repo. I think that benefit has already come to us. But what we will definitely look forward to is the reduction in the MCLR by the banks. And most of the proposals in the banks, it gets renewed in the second quarter of the year once the financial results are out.

So, I think going forward we should look at 20 to 25 basis points reduction in the overall cost. And the incremental cost should even come down further. Add to that, we will also be doing

more offshore. Offshore comes at significantly lower cost. We have good sanctions in our hand. And I think that is something that we should capitalize on in the next couple of months.

- Ashish Mehrotra:** It should reflect in our margin.
- Atul Tibrewal:** So that would definitely add to the NIM expansion, coupled with the better yield from year on.
- Chintan Shah:** So that's quite in detail. So, one thing on the guidance front, so as such means, so considering the credit cost, we have guided for 270 to 290 bps in this year. But so, what kind of credit cost do we expect in FY '27 as well? So here the credit cost should be on a downward trajectory. So, can it settle around 2.5% or like how should we look at it from a steady state perspective?
- Atul Tibrewal:** So, as you know, our mix would be changing. As the asset mix changes in favor of direct to retail, we will have a higher amount of credit cost. So, we will be in the range of 2.7% to 2.8% in FY '27. But '28 onwards, I think we should see a slight reduction to around 2.5% to 2.6%. That is how we have given guidance in the past as well and we stick to that guidance.
- Pardhasaradhi R.:** Just to add to that, obviously with the mix change, there will be expansion in NIM as well and that sufficiently covers the increasing credit cost.
- Chintan Shah:** Yes, sure. So, from a ROA standpoint, so in FY '27, can we be looking at around 3.5% ROA or how is it?
- Atul Tibrewal:** Yes, we should be looking at those numbers and that is how we should reach close to 4% by FY '28.
- Chintan Shah:** Sure, that is very helpful. I'll join back in Q&A. Thank you and all the best.
- Moderator:** Thank you. That was the last question for today. I now hand the conference over to the management for closing comments.
- Ashish Mehrotra:** Thank you all very much. Thanks, Chintan. Thank you, moderator, for really managing it well. Thank you all for joining late on Tuesday evening. I really appreciate your support and very insightful questions. Have a great day and a great year ahead. Thank you.
- Moderator:** On behalf of ICICI Securities Limited, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.