"CreditAccess Grameen Limited Q3 FY2022 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to CreditAccess Grameen Limited's Q3 FY2022 earnings conference call hosted by IIFL 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 '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Arash Arethna from IIFL Securities Limited. Thank you and over to you Sir!

Arash Arethna: Thanks Janice. Firstly, I would like to thank the management for giving us the opportunity to host this call. From the management side, we have Mr. Udaya Kumar Hebbar, Managing Director and CEO, Mr. Balakrishna Kamath, CFO and Mr. Nilesh Dalvi, Vice President of Investor Relations. Let me now hand over the call to the management for the opening comments and post that we can proceed to open the floor for Q&A.

Udaya Kumar Hebbar: Thank you. Good morning friends, our sincere thanks to everyone for taking your time this morning and joining us today to discuss our third quarter and first nine months financial performance. At the outset, we are happy to inform you that we have been again certified as "Great Place to Work" successively for the third time. This reinforces our strong work culture, employee centricity, and commitment to reach greater heights in the future.

Coming to our business, we witnessed significant improvement in our financial performance during the third quarter backed by sustained business momentum and consistent improvement in asset quality. Strong portfolio growth, lower delinquencies, and improved bad debt recoveries led to a sharp improvement in operating profitability. We have reclaimed our quarterly PAT of more than Rs.100 Crores after two years. Our monthly disbursement run rate at CA Grameen further improved from over Rs.1,100 Crores in September to over Rs.1400 Crores in December. All new disbursements across all states since June 2021 are displaying very good quality with a current PAR 1-30 of only around 1% with limited flow forward. MMFL is also back into growth trajectory and all new loans are disbursed under the CA Grameen model since October, amounting to over 45% of the book and showing very high asset quality comparable with CA Grameen.

As indicated earlier, the monthly disbursement at MMFL also doubled from Rs.180 Crores in September to Rs.360 Crores in December. We are back into a growth trajectory in terms of disbursement and growth in MMFL now. At a consolidated level, we disbursed Rs.4,720 Crores in Q3 FY22 and acquired over 2 lakh new borrowers. Over the past 12 months, we acquired over 5.4 lakh new borrowers out of which 48% were from outside of the top 3 states as we continued to go deep rural and expand our presence in newer markets. We

continued to witness MoM reduction in delinquencies during third quarter. At CA Grameen, collection efficiency excluding arrears rose from 93.3% in September to 95% in December and further to 95.6% in January. Excluding non-paying NPA customers, collection efficiency excluding arrears touched 98% in December and 99% in January. The collection efficiency in MMFL, which constitutes 16% of our consolidated GLP gradually improved from 87% in September to 89% in December and 90% in January. Excluding non-paying NPA customers, collection efficiency excluding arrears touched 91% in December and 92% in January at MMFL. At CA Grameen, the asset quality maintained the improvement momentum as PAR 30 reduced from 8.5% in September to 5.4% in January and PAR 60 reduced from 5.4% in September to 4.2% in January. Similarly, at MMFL, PAR 30 reduced from 13.4% in September to 10.7% in January and PAR 60 reduced from 10.3% in September to 8.5% in January.

On a standalone basis, our gross loan portfolio grew by 19.4% Y-o-Y and 8.9% Q-o-Q to Rs.12,180 Crores in Q3 FY22. However, the borrower base declined by 1.9% Y-o-Y to Rs.28.14 lakhs, primarily due to write-off of over 2 lakh borrowers during the last 12 months as well as lesser new acquisitions in the first 6 months of this financial year. However, on Q-o-Q basis, the borrower base increased by 60,000 in Q3 FY22 as we added over 1.8 lakh new borrowers partially offset by a write off of over 47,000 borrowers in Q3 FY22. The NII grew by 40.4% Y-o-Y to Rs.349.4 Crores while NIM stood at 11.7%. Adjusting for the impact of interest income de-recognition and the impact of maintaining higher liquidity on the balance sheet, NIM would have been at 12.4%. The cost to income ratio was at healthy 36.1% while Opex to GLP saw a reduction at 4.7%. PPOP grew by 67.1% Y-o-Y to Rs.245.6 Crores. The credit cost was Rs.73.8 Crores which also included the impact of write-off of Rs.134.9 Crores. The credit cost was partially offset by Rs.26.8 Crores bad debt recovery during the third quarter. PAT for the third quarter was Rs.129.2 Crores leading to ROA of 3.8% and ROE of 13.6%. GNPA (@ 60+ dpd) reduced from 7.18% in September 2021 to 5.5% in December 2021. Overall ECL stood at 4.4%.

On a consolidated basis, our gross loan portfolio grew by 18.4% Y-o-Y to Rs.14,587 Crores and the borrower base declined by 4.3% Y-o-Y to 37.39 lakh, primarily due to write off of 3.91 lakh borrowers during the last 12 months. NII grew by 35.5% Y-o-Y to Rs.412 Crores. PPOP grew by 60.6% Y-o-Y to Rs.273.5 Crores. The credit cost was Rs.117.9 Crores which also included the impact of write-off of Rs.190 Crores. The credit cost was partially offset by Rs.29.2 Crores bad debt recovery during the third quarter. PAT was Rs.117 Crores, resulting in ROA of 3% and ROE of 11.9% on a consolidated basis.

Briefly touching on our financial performance during 9M FY22 on a consolidated basis, our NII grew by 11.4% to Rs.1,133.6 Crores. PPOP grew by 13.8% Y-o-Y to Rs.708.7 Crores.

Credit cost declined 14.4% Y-o-Y to Rs.445.7 Crores, and bad debt recovery was robust at Rs.47.6 Crores in 9M FY22. While the gross credit cost in 9M FY22 was 3.6%, the net credit cost after considering the bad debt recovery is 3.2%. PAT grew by 162% to Rs.197 Crores resulting in ROA of 1.7%. Liquidity continued to remain comfortable with total cash and cash equivalents of Rs.1,625 Crores amounting to 10.3% of total assets. Capital adequacy remained strong at 24.8% at a consolidated level. With field integration completed, portfolio transitioning into CA Grameen model along with growth momentum picking up with speed in MMFL, we believe that positive bottom-line contribution will follow going forward in MMFL also. We continue to maintain our focus on foraying into newer rural markets as part of our geographical diversification strategy and tap the unserved and underserved markets. A total of 193 branches have been opened during this financial year, primarily across the newer markets. Our overall branch network stands at 1,617 as on January 31, 2022. With improved visibility on the business environment on the back of reducing the severity of the pandemic and increasing vaccination, we had provided performance guidance for FY 2022 in the last quarter.

As of 9M FY22, we are happy to inform that our performance has been fairly in line with the guidance. While the country did face temporary challenges on account of Omicron variant during January, our business remained unaffected without any disruptions. In fact, key indicators like portfolio growth, customer base, collections, and asset quality further improved in January compared to December. Happy to note that we also achieved a major milestone with our consolidated loan portfolio crossing the USD 2 billion mark in January. Assuming that there are no further severe business disruptions on account of COVID, we are confident of achieving our guidance for FY 2022. Our learning from previous waves and the pragmatic approach adopted give us enough confidence to weather the odds. The government has made its stance clear during the budget 2022-23 with capital expenditure push and inclusive development agenda being the drivers of creating long-term job opportunities for millions of low-income households. Given our strategic position of deep rural presence, we are proud to partner in this growth journey and contribute towards the next level of the capital creation story of Bharat. With this brief note, I would like to open the floor to you for any questions. Thank you.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question-and-answer session. The first question is from the line of Shreepal Doshi from Equirus Securities. Please go ahead.

Shreepal Doshi: Good morning and thank you for giving me the opportunity. Firstly, if you look at January, the non-paying customers have increased versus the December numbers for both Madura and CreditAccess. So, what would be the reason for the same?

Udaya Kumar Hebbar: There is a small momentum that is already there in the NPA category which is more than 90 days or 180 days. There is a slight fast forward over there. It is already NPA and provided customers, so some of them have not paid during January. There is no paying customer in the standard category mode by that side.

Shreepal Doshi: This is broadly the partially paying moving into nonpaying?

Udaya Kumar Hebbar: Yes, some of them that would have paid in December, they may not have paid in January. They may have paid in February, particularly most of them are more than 90 days or 180 days bucket customers.

Shreepal Doshi: Got it Sir and you have given a split of ticket sizing, vintage-wise ticket size. So, if you could also give us a split of customers as per the vintage, in a similar category wherein below three years, three to six years, six to nine years and more than nine years?

Udaya Kumar Hebbar: We have given that.

Shreepal Doshi: If you can give the customer split also like we have given ticket size, so if you can give customer split also?

Udaya Kumar Hebbar: Actually, we have a portfolio split available on the top of the slide. It largely reflects the customer borrower split also, maybe we can provide that. Nilesh can provide that because the portfolio split is there in the top bar in the same slide. So, the number of customers are slightly varied because the high vintage customers have higher portfolio. So, there will be a slight variation maybe we can provide it next time or you can reach out to Nilesh he can get it. Thank you.

Shreepal Doshi: As highlighted in same slide, 40% of the customers are new which are from non-core states for us. So, these will be Bihar, UP, Gujarat, Rajasthan?

Udaya Kumar Hebbar: Yes, by and large other than the three core states and largely from Bihar, Jharkhand, UP, Gujarat, Rajasthan and Odisha.

Shreepal Doshi: What is the ticket size that you are beginning for these customers in this geography?

Udaya Kumar Hebbar: If you see the same slide right side corner, it is mentioned that the outstanding in the other states average is only Rs.32,000.

Shreepal Doshi: But what would be the beginning like the first cycle?

Udaya Kumar Hebbar: Beginning is Rs.30,000 to Rs.35,000.

Shreepal Doshi: I will come in the queue if I have more questions. Thank you so much.

Moderator: Thank you. The next question is from the line of Siddharth Gupta from CreditAccess. Please go ahead.

Siddharth Gupta: I just wanted to know what does the company expects the credit cost to be next year in FY23?

Udaya Kumar Hebbar: We have guided in Q2 itself on the credit cost which will be overall between 4.2% to 4.7%. So, we should be within that.

Siddharth Gupta: No, I am talking about the next financial year. What is your guidance for credit cost for the next financial year?

Udaya Kumar Hebbar: Next financial year we are not able to guide right now. Probably we will look at Q1 and after we will be able to guide. So, we believe that majority of the COVID cost impact would be taken now. Therefore, it should be business as usual. but there would be little higher cost considering the behavioral change of the customers at this point of time. But we presume that it will be at least 70-80% more than normal. Anyway, we will provide it after Q1.

Siddharth Gupta: Okay and do you expect any write-off due to third Omicron wave?

Udaya Kumar Hebbar: No.

Siddharth Gupta: Okay.

Udaya Kumar Hebbar: Not for the third, there is no impact from the third Omicron wave.

Siddharth Gupta: Thank you.

Moderator: Thank you. The next question is from the line of Digant Haria from GreenEdge Wealth. Please go ahead.

Digant Haria: My first question is on these harmonization guidelines. If they come, do you have a chance to correct our lending rate because I believe at a lot of places we are lending at rates that are even lower than the banks?

Udaya Kumar Hebbar: Definitely if there is an opportunity for us, we should be pricing for the credit cost. As of now, we are the lowest priced as against banks, NBFCs, NBFC-MFIs, and everybody in the entire market. We are the lowest-priced MFI today. However, because currently, we are constraint with a 10% margin cap of RBI, we are not able to price for the cost of credit which is much higher in some markets. So, definitely if the opportunity is given by the regulation we should be definitely charging the credit cost to some extent and at least to price the cost if possible.

Digant Haria: In that opportunity, would it be between 50 to 100 bps or a little more? Just a ballpark number, do not need an exact number.

Udaya Kumar Hebbar: It should be between 100 to 150 bps on some of the geographies.

Digant Haria: The second question is mainly on the field operation with regards to COVID because of this being a highly physical touch model and the attendance had suffered in the first few months of COVID. So, now do you think that those disruptions are really behind? Or has the customer behavior changed in such a way that the from group model eventually a lot of people be forced to migrate to individual models? And basic question is, in FY23 can we look at normalcy like no COVID disruptions and physical touch comes back?

Udaya Kumar Hebbar: It is already back to normal. Only those groups were one, two, or three defaulted customers, in such a center some discrepancies are there. The customer who are paying, more than 75%, 80% of the groups are paying full and normal. The behavioral and discipline are by and large normal. So, we do not see any challenges there.

Digant Haria: Okay.

Udaya Kumar Hebbar: It is only improving going forward.

Digant Haria: My last question is on the growth. Because so many customers are either under restructured or PAR or NPA for other MFIs and other bank MFIs also. Does it put a strain on our own growth pool that may be the next year even it is a normal year we would have grown 25%. But is there availability of customers because the Experian data would show that there are overdue somewhere or restructured somewhere. So just any thoughts on that? That's it from my side.

Udaya Kumar Hebbar: We as an institution keep expanding in deep rural and beyond the urban also. Our fair target is always to bring new to credit customers into microfinance and support them for their own growth. If you see last year or at least stable years, our new to credit customers was almost

40% to 45% when we acquired the new customers. So, even now also we believe we will be able to target the new to credit customers more, and not necessarily we should go and lend to the customers who defaulted. So, there is an opportunity. If you see today only 35-40% of the addressable market has been achieved by the industry. So, there is a huge 50% of non-addressed market available in the geographies where you operate and particularly in rural. Therefore, we do not see a challenge for growth considering there are some delinquent customers at this point of time, which is also only 20%. If you count 6 Crores customers currently, even if 20% of customers are delinquent in between, there is still 80% that are not, and still there are others new to credit. I think we do not see any challenge about the growth, the highway is still available.

Digant Haria: Okay, great Sir. All the best for the coming quarters. Thank you.

Moderator: Thank you. The next question is from the line of Nidhesh Jain from Investec. Please go ahead.

Nidhesh Jain: Thanks for the opportunity, Sir. Firstly, on the income from the recovery that we have reported this quarter is quite strong at Rs.29 Crores. How should we think about this income going forward? What is the write-off pool on which we are trying to recover?

Udaya Kumar Hebbar: Nidhesh what happened is, the denominator also increased this year because, in the last nine months, we have written off both combined together almost close to Rs.398 Crores. I think at least for the next two, three quarters we should see Rs.15-20 Crores of recovery because that is the natural trend. When you write off 270 days, we wrote off even some of the partly paying customers also because of the policy of writing off at 270 days. So, obviously, there will be recovery from those customers also. Some of the customers who want to come back or those who want to borrow from some others have to come and pay us before doing that. We have to put a large team to adjust this, to go and meet all the delinquent customers. Also, recollect that we did some aggressive or early write-off also at 180 days sometime. So, there is an opportunity to go back and collect some money. In our sense, at least for the next two-three quarters, we should be able to recover at least Rs.15-20 Crores every quarter.

Nidhesh Jain: Secondly Sir, from a number of customers perspective, the number of customers has remained flat or declined over the last two quarters because of write-off that we have been doing. But from the next two to three years perspective, how should we think about the customer base growth for the company?

Udaya Kumar Hebbar: It is growing already. As I said in the initial remark from Q2 to Q3 we have grown already. We are acquiring almost close to 90,000 customers every month now. So, maybe there is

one more write off a large number. Probably, Q4 would impact a bit but afterward, it should only be positive every Q-o-Q, Nidhesh.

Nidhesh Jain: Sure, so this 90,000-customer addition will be sustainable on a monthly basis?

Udaya Kumar Hebbar: It should be because we have created good infrastructure like almost 200 odd branches we added already with the existing branches. Normally in Q1 and Q2, we will open fresh branches every year. Given that there are no disturbances, we should be going ahead and keep opening 10-15% of infrastructure every year. This will also give additional support for customer growth.

Nidhesh Jain: That is it from my side.

Moderator: Thank you. The next question is from the line of Anand Bhavnani from White Oak Capital. Please go ahead.

Anand Bhavnani: Thank you for the opportunity Sir. Just wish to understand over the last seven, eight quarters, as you are expanding into newer geographies and even in existing geographies. How is the competition intensity as compared to pre-pandemic? Have you seen any changes in the competitive intensity post the pandemic?

Udaya Kumar Hebbar: Last eight quarters cannot be compared because of the disturbances. By and large if you see the eight quarters, at least in four quarters nobody operated. Six months in FY2021 and six months in 2021-2022. So, there was no expansion by anybody. It was more of fighting with the pandemic issues. So, it is not comparable, but still real growth for the industry came only during the second half in both the last two financial years. But having said that, it is important to note that we are a deeply rural penetrated institution which is having very less competition compared to the urban penetrated institutions. Just to give you an example, we have a large number of MFIs and banks operating across geographies. To put it in perspective, for almost 43% of customers we are the only lender. For another 39% of customers have only one lender other than us. So, that itself shows that the competitive intensity in the field is not impacting us. To give the other side of the reflection on who is the largest overlap with us in terms of common customers. We have Bharat Finance which is one of the largest, almost double of our size has only 8% of overlapping. The next overlap is Spandana about 5% to 6%. Thereafter, may be Bandhan which is about 3% of overlap. So, by default, the design of our operation is such that we are not susceptible for a large competition because of our deep rural presence and our tendency of acquiring new to credit customers. Probably I answered your question.

Anand Bhavnani: Sure Sir that is very helpful. The second part is if you were to look at the industry over the last seven, eight years, a lot of firms were funded by private equity. Now because of the sequence of events that has happened since 2016, the rate of return for a lot of private equity players in microfinance in India are subpar and some of them are not even able to get exits. So, with respect to fresh capital, are you seeing that private equity is reluctant when you see as an industry participant? I want to understand the competitive intensity. So, is incremental funding from private equity lower, and do you see it staying low for the next few years?

Udaya Kumar Hebbar: Anand if you see despite pandemic last year, sufficient equity has flown to microfinance and it is not suffering from any equity shortage today, despite two years of all these problems. That itself validates that there is enough interest of capital flowing into the industry. There are banks, there is government support and RBI has come with plans. So, I do not think there is an issue about equity or about funding for the industry. The industry has grown continuously. Whether it is two years or four years or six years, if you see the industry has grown leaps and bounds. So, I do not see any challenge about equity raising today for anybody. When they are able to raise equity even in the pandemic years, I think it reflects the strength of the industry.

Anand Bhavnani: Sure Sir, my question was more for our peers because I understand we are able to raise equity?

Udaya Kumar Hebbar: I am also telling about the industry, not Grameen. There is not one institution that suffered because there is no equity today even after two years of the pandemic. So that is what I am telling.

Anand Bhavnani: Got it Sir and last question if I may, do we have any sense, when can we expect these new regulations which is now almost eight, nine months since we are contemplating this. Do we have any sense when can we expect some final decision on this?

Udaya Kumar Hebbar: Both of us are in the same information stage, so we also do not know. We expected this in the last quarter itself, but somehow not yet. Let us see it maybe RBI would have more other priorities probably. But it should be coming this quarter that is what we are hoping.

Anand Bhavnani: Okay and Madura is on track to be merged by end of the current quarter that is Q4 FY22 right?

Udaya Kumar Hebbar: Not necessarily. The legal merger might take more time because of the regulatory issues, which NCLT hearings have taken time because of COVID. And they do not have sufficient

bandwidth to manage the pending cases. But from our own perspective, we are already integrated, from an operational perspective, product perspective, growth perspective. We may still have to carry two boards for some more time.

Anand Bhavnani: Noted. Thank you, Sir. I will come back in the queue.

Moderator: Thank you. The next question is from the line of Kartik Sahni from Myriad Asset Management. Please go ahead.

Kartik Sahni: Good morning. I just want to ask what is your guidance on the loan book growth in the next two years?

Udaya Kumar Hebbar: Despite pandemic years, last year we grew 13% to 14%. This year we guided to grow almost 17% to 19%. So, we believe that this can be little more than this on a stable year going forward. At least 20-25% CAGR for the next three years which is potential for the industry.

Kartik Sahni: Thank you so much.

Moderator: Thank you. The next question is from the line of Amit Nanavati from Nomura. Please go ahead.

Amit Nanavati: Just a couple of questions on write-offs. Firstly, if I look at our PAR splits right now we have nearly kind of normalized and when you look at non-paying customers is more or less crystallized. So, to that extent, should one expect the non-paying customers largely to be written off over the course of the next two quarters? Or if you can just explain some behavior around that, what we expect to recover hopefully over some time?

Udaya Kumar Hebbar: We expect a majority of this should be written off in the fourth quarter itself or maybe some may spill over to Q1 also. But your estimation is correct, to large extent the non-paying NPA will move. But as a policy, we write-off all the customers if the NPA or delinquency bucket crosses 270 days. So out of our current PAR 90, largely might be getting written off in Q4 and Q1. You are absolutely right.

Amit Nanavati: Okay, so regarding credit cost guidance, if I look at it on an incremental basis it will be largely towards the write-off requirement?

Udaya Kumar Hebbar: Absolutely, you are right.

Amit Nanavati: If you can only explain in terms of write-offs that we have done in the past 12 months, what would be the similar vintage split of borrowers that you would have written off? Basically, in terms of ticket size and in terms of vintage. How was this broad split around less than three years, three to six years or more than nine years etc.?

Udaya Kumar Hebbar: We have not done that. Probably we will publish that too. You can reach out to Nilesh and he will be able to collate the data and share with you. But we have not split the vintage of write off the number at this point of time, probably we can do that. Nilesh do you have any specific data available on this?

Nilesh Dalvi: I will provide it to him, currently I do not have it.

Amit Nanavati: But broadly Sir, if you can just on the top of your head, if you would have seen any stark difference whether the write-offs are a low vintage customer or high vintage customer?

Udaya Kumar Hebbar: Amit, actually our write-offs are linked to pandemic today and not the vintage. You cannot correlate the vintage versus write-off because this is a specific event which impacted the customers who are not in the essential activities or suffered specifically because of the low footfall kind of business, which we already discussed earlier. What kind of business was impacted in the last two COVID situations irrespective of whether it is a new vintage customer or old vintage customer. It is more of an industry and specific customers who are impacted actually. The customer could be five years also, one year also but if she or the family is running salons or they are in travel or tourism or pilgrimage centric, they are impacted. It may not be a right data to see based on vintage or non-vintage. It is more of essential and nonessential or the key in terms of the impact and the resultant write-off of last four to five quarters. Anyway, I think Nilesh can provide that data, but we cannot derive any decision based on that because of these other external reasons.

Amit Nanavati: Got it sir. That is it from me. Thank you.

Moderator: Thank you. The next question is from the line of Anand Bhavnani from White Oak Capital. Please go ahead.

Anand Bhavnani: Sir just a couple of questions, one is on Madura. You mentioned we have now integrated. In COVID, we saw there was a stark difference in the credit quality and maybe it was due to the legacy book. But since the legacy book has completely runoff in the last couple of years, from hereon we should expect broadly the performance to be similar barring some geographical disturbances. But barring that, broadly the loan book performance should be in sync with CreditAccess?

Udaya Kumar Hebbar: Anand only 45% of the book is a new book and of the Grameen model. 55% still the old and yet to run off and it is going on. Actually, we are not disbursing anything under the old model, everything is according to the new model, which is exactly behaving the way Grameen is behaving. But if you see Madura's write offs are with the lag compared to Grameen. We have taken write off early whereas Madura's write off comes later because it is a different kind of model so recovery happens slowly there. That is why write offs have started now only there. So, it will take maybe two to three quarters to breakdown those delinquencies, which we are not able to recover. Maybe next two quarters, we will receive some data. But still, we believe that the current growth momentum will help us to generate enough revenue to take such costs and we should be still positive in employing the Madura book also from here onwards.

Anand Bhavnani: Okay, wondering we took over the company in Q3 or Q4 of FY2020. So, it is close to 24 months now and generally, the loans are for that tenure. So, I am surprised by the 55% figure being the legacy book because it would run off right? The books run off very sharply in microfinance so how come we have 55% still?

Udaya Kumar Hebbar: Anand we are in the middle of COVID. We are not in the normal stable period. We are not able to go and implement technology and all those things. It always needs a year to integrate and in one year we have done the integration. And the new business, new book under the model change is not easy for the old book. Old book has to run off, so new book under the model started in October 2021. We would have started in March, but again COVID wave 2 impacted us so we had to postpone that and we started in September-October 2021. So there afterward the new book built is 45% now. So old book has to run off, it is a process. We cannot just convert the book into a model as it impacts the customers there. So, we have taken a very pragmatic approach in doing it and we believe what we did is right.

Anand Bhavnani: Sure. Any ballpark expectation you have for write-off in Madura for the next two to three quarters as you said any sense you can give us on that?

Udaya Kumar Hebbar: No, you have the data in front of you about the NPA and whatever we have, we have provided about it right. Write-off will not impact the book directly right, it is only the non-provided component that is impacted. So, we have taken the recognized NPAs and provided against it.

Anand Bhavnani: Sure. In terms of the expansion plan we added quite a bit of branches in the last two years. How do you see branch addition going forward let us say next couple of years?

Udaya Kumar Hebbar: So, we keep taking stock at a point of time. Normally we add branches if you see the history, we add about 10% to 15% infrastructure every year which includes the number of branches, employees and everything. So probably, we will be going in a similar direction.

Anand Bhavnani: Noted. Thank you, Sir and good luck. I will come back in the queue for any question.

Moderator: Thank you. The next question is from the line of Abhishek Murarka from HSBC. Please go ahead.

Abhishek Murarka: Good morning and congratulations for the quarter. Sir the question is on Madura. So, this new book and old book split that you have given, this is from what date? Are you counting from the date of our first investment?

Udaya Kumar Hebbar: When I said new book, I said book which is built in the Grameen model not the new book within Madura. So, we have shifted the model and transitioned to our own technology which is a weekly/fortnightly model. So that book is 45%. Madura itself kept on disbursing money so that the new book perspective is slightly different, but still it is the old model. You are absolutely right. The new technology, new process, and new product, new weekly fortnightly model started in October is the book I am telling. This is exactly the Grameen model.

Abhishek Murarka: Right so basically October, November, December, January, those four months is 45%?

Udaya Kumar Hebbar: Yes exactly. Every month almost 10% is getting shifted Abhishek.

Abhishek Murarka: Okay, perfect, that is what I thought Sir. And the other thing is, going forward what is the business as usual credit cost that we are estimating? If I look at pre-demonetization, our long period average was 1.5%, post demonetization now it is coming to 2% to 2.5% so where are we looking at average business as usual credit cost?

Udaya Kumar Hebbar: Pre-demonetization it was 50 to 80 bps not even 1.5% actually. Post demonetization it went about 120 to 130 bps actually. So, we believe it will again increase further by 50 to 60 bps going forward because of this important behavioral change. In fact, because of two years of COVID, there were moratoriums, there were restructures, so many things are there for the industry and the customer also. So, based on this there would be some behavioral change which will impact the overall discipline and the repayment behavior. We believe it will be an additional 50 that is 150 to 180 bps maybe your business as usual going forward.

Abhishek Murarka: Are you able to still pass on a higher yield? One of the impacts of harmonization was expected to be that an NBFC MFI will migrate to a 22-23% yield. So, are you able to charge anything higher?

Udaya Kumar Hebbar: We are expecting that because one of our reasons for reaching out to RBI is to consider the credit cost for the pricing actually and that is what RBI recommended in their draft guidelines. So, we believe it will be implemented as soon as possible and it will give us leverage to price the cost.

Abhishek Murarka: Right.

Udaya Kumar Hebbar: Still, we should be able to give stable returns to the investor.

Abhishek Murarka: Finally, on retail finance, three to four years back when we started, we had a lot of plans for it. In the last two years, it has clearly been drawn down and it is just about 2%. But going forward, what is the plan for that book?

Udaya Kumar Hebbar: Correct. So, the acquisition impacted the retail book indirectly actually. The investment what we made in Madura was treated as non-microfinance book because of the non-qualified asset. That is why we did not have headroom to grow in the retail book. In any case unsecured book, we did not want to grow also slowly because we realized that this kind of event will hit the individual microfinance book so definitely it is not a good idea. After these two waves actually, we learned a lesson on this that is why we started reducing the portfolio now it is only 2%. But the plan is to move towards the secured book. So, we are already working on various pilots I think last time also I appreciated this. We are working on a business loan backed by assets particularly properties, affordable housing, home improvement, gold loan, two-wheeler loan. All these are being worked out. We are actually building the team, developing the technology, and creating a pilot to learn the new sensors. So, my sense is we will have very good traction in FY2022-23 on these assets. By the time we complete the legal integration, we will get headroom to grow also. So, before that, we will be ready with our pilots so that we can grow our secured book. Our target is to use the opportunity of the non-microfinance portfolio as a secured book going forward so we are working on that.

Abhishek Murarka: Any milestone let us say two years out where this 2% should go maybe targeting 4%, 5% any milestone that you have in mind?

Udaya Kumar Hebbar: In the next two years, by 2024 we should be crossing 10% to 12% in this.

Abhishek Murarka: 10 to 12% sorry?

Udaya Kumar Hebbar: By 2024, we should be achieving about 10% to 12% of our book as a secured book.

Abhishek Murarka: Of the overall GLP?

Udaya Kumar Hebbar: Correct overall GLP. We are currently 13% to 14%. We cannot do more than that because 85% has to be qualified right. So, at least 10% to 12%, then the balance will be our normal balance sheet assets.

Abhishek Murarka: Okay, understood Sir. Thank you for taking my questions. All the best.

Moderator: Thank you. The next question is from the line of Rajiv Mehta from Yes Securities. Please go ahead.

Rajiv: Many congratulations on very strong numbers. Sir just one question from my side, you spoke about the new normal of credit cost being 1.5% to 2% going ahead. But when I look at your January collection efficiency on the paying customers including some overdue customers as well as some NPA customers who are paying, it is 99%. So, why do you think that your incremental credit cost in a normalized environment will be higher at 1.5% to 2%?

Udaya Kumar Hebbar: So, we need to see Rajiv going forward it may not be entirely stable as we have seen before 2016. And we are now across geographies. There are floods, there is something else, and these are going to be common. A very good and stable one month cannot be a reflection of our entire future. So the behavioral change is the one that will impact. 99% is good for the non-paying customer but still, you have other customers who have defaulted also right. Almost 5.4% of customers are still there right. So, one month is great but not necessarily all the months. On a regular basis, this could be 1.5%, not 2%. It may be about 1.5% which will be our stable business credit cost because credit cost is not just the write-offs. Your target credit cost is including the provisions. The standard provisions itself is close to 1% right so any addition will become ECL more than 1.5% to 2%. If you remember before COVID when everything was stable, our ECL was almost 2% because standard itself we provide almost 1% right. So, credit cost is including your provisions.

Rajiv: Sir in this stage 2 we are holding 20% provision right now and of course, stage 3 is 60%. But a lot of it will get written off then we will also build provisions in the fourth quarter. Stage 2 on a steady-state basis, what is the kind of provision we would typically hold? Would we want to hold 30% on a stage 2 book going ahead?

Udaya Kumar Hebbar: It will be between 30% to 40% on a stable basis. Currently what is happening in stage 2 Rajiv. A large number of them are paying more than 50% of the due. That is why we have provided a little less there currently. It is three buckets within stage 2. One is non-paying, one is paying less than 50% of the due and the other is paying more than 50% of the due. So, because of that it is becoming around 20%. But on a stable basis, it will be 30% to 40%. But stage 2 will not be that high also because of 15 to 60 days only right, so it will be quite low going forward.

Rajiv: The overall quantum will go down.

Udaya Kumar Hebbar: Correct.

Rajiv: Thank you Sir.

Moderator: Thank you. The next question is from the line of Madhu Gupta from Quantum AMC. Please go ahead.

Madhu Gupta: Actually, most of my questions have been answered just one question the company has received an IT notice of around 23.3 billion for the year FY19, so any updates on that?

Udaya Kumar Hebbar: Madhu we have updated this on January 21, 2022 to the exchanges. So, the High Court of Karnataka heard that case between us and the income tax and they have set aside the order at this point of time.

Madhu Gupta: There was an interim stay on that so that is still continuing?

Udaya Kumar Hebbar: Earlier it was a stay, now the order itself is set aside by the court.

Madhu Gupta: So that means the company does not have to provide for the contingent liabilities?

Udaya Kumar Hebbar: Yes, even before also the tax experts clearly told that there is no need to provide, but now that order itself is set aside so there is no need for new provisions.

Madhu Gupta: So, in a way sort of the company has won the case in a way that means the liability will not arise in future is that the understanding?

Udaya Kumar Hebbar: See it will go back into the income tax department. And they may have to relook at the case and then they will come back and then we will pay appropriately to them. There is no demand at this point of time.

Madhu Gupta: At this point of it is not there, got it, thanks.

Moderator: Thank you. The next question is from the line of Abhishek Murarka from HSBC. Please go ahead.

Abhishek Murarka: Thanks for taking the follow-up. Our marginal cost of borrowing is now quite low, but incrementally how much of your borrowings mature in this year and given the TD rates, etc., going up what is the general borrowing plan for 2022-2023?

Udaya Kumar Hebbar: Short-term borrowing is already available in the slides actually. We have put in the bucket of short, medium, and long. So, I think about 10% only is short-term borrowing which is less than 12-month maturity I agree that we have more than 45% for more than three years bucket actually. The interest hardening is potentially there but considering that we have good line of credit from the banks at lower cost and the legacy costs are a little higher. On an average basis, it should not increase too much, the variant maybe 10% to 15% considering the next two to three-quarters point of view. So, we do not see too much variation on the average cost of borrowing for us.

Abhishek Murarka: Okay so the gap between marginal and weighted average at 1% it will still take some time to converge?

Udaya Kumar Hebbar: Yes, it will take time.

Abhishek Murarka: Got it, thanks Sir.

Udaya Kumar Hebbar: Currently, our weighted average is around 9.1% or so. So, maybe even if a little hardening at least for the next two to three quarters it can be a 15-bps variation potential, not more than that. Because of the legacy borrowings which are being paid out and the new borrowing you are getting at a lower rate, on average it will be between 9.1 to 9.3.

Abhishek Murarka: Within your bank borrowing how much would be linked to any external benchmark?

Udaya Kumar Hebbar: No other. Only the external borrowing about 10% to 11% is linked to LIBOR, that also annual reset, which is hedged. The LIBOR can change and reset can happen that also is hedged actually. And the domestic maybe about 45% to 50% odd floating with the floating to MCLR.

Abhishek Murarka: Okay, but non-MCLR external benchmark in the case of domestic is very low?

Udaya Kumar Hebbar: No, insignificant.

Abhishek Murarka: Got it Sir, thank you.

Moderator: Thank you. Ladies and gentlemen that was the last question for today. I would now like to hand the conference back to the management for their closing comments.

Udaya Kumar Hebbar: Thank you very much for joining this call and we appreciate all the questions. We hope we were able to give you clarity, in case anybody has further questions for the data requirement please reach out to our investor's desk so they will help you. Thank you very much. Have a nice day.

Moderator: Thank you. On behalf of IIFL Securities Limited we conclude today's conference. Thank you all for joining, you may now disconnect your lines.