"Ujjivan Small Finance Bank Limited

Q3 FY '23 Earnings Conference Call"

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MODERATOR: **MR. ARASH ARETHNA – IIFL SECURITIES LIMITED –**

Moderator: Ladies and gentlemen, good day, and welcome to Ujjivan Small Finance Bank Limited Q3 FY ’23 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 star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Arash Arethna from IIFL Securities Limited. Thank you, and over to you, sir.

Arash Arethna: Yes. Thank you to the participants for joining and thanks to the management of Ujjivan Small Finance Bank for giving us the chance to host this call. From the management, we have Mr. Ittira Davis, MD and Chief Executive Officer; Ms. Carol Furtado, Chief Business Officer; Mr. M. D. Ramesh Murthy, Chief Financial Officer; Mr. Martin P. S., Chief Operating Officer; Mr. Ashish Goel, Chief Credit Officer; Mr. Vibhas Chandra, Head of Micro Banking; and Mr. Deepak Khetan, Head Financial Planning, Strategy and Investor Relations.

I’d now like to hand over the call to the management for their opening comments, post which we can move on to Q&A. Thank you.

Ittira Davis: Thank you. Good evening, and welcome to our Q3 Financial Year ’23 Earnings Call. It gives me immense pleasure to share with you that we just turned six. This is our sixth anniversary. It is an important milestone for us, because today we serve 7.3 million customers through 607 branches and an employee strength of 17,000. These six years have been a mixed bag of learnings and achievements in our journey towards becoming a leading mass market bank. Q3 has been another good quarter for Ujjivan, as it marks more than 12 months of being profitable after a rough patch. Another update is, RBI extending my tenure as MD.

During this period of the extension, the Board would identify potential candidates and they would work with me for a smooth transition to take the Ujjivan journey forward. Coming to our Q3 performance, it was an all-around performance with strong disbursements, gross loan book growth, and an even better deposit growth. Collection continues to be good and credit quality has improved further. This quarter, even post-implementation of the new credit MFI norms, we disbursed INR 4,838 crores and almost another record from the previous quarter.

The system took a little while to settle down with the new norms but now all is back to normal.

In fact, December ’22 was the highest ever monthly disbursement for Ujjivan. Our gross loan books grew 5% sequentially to INR 21,895 crores after total write-off of INR 179 crores. While overall, all asset businesses performed well. You would have noticed a small decline in the MSE book. This is in-line with what we have been mentioning since the last two calls that we are adjusting our strategy there and we’ll see growth once all changes are in place, and systems also upgraded for that.

Asset growth was outpaced by the growth of our deposits, which grew at 14% sequentially, registering the highest ever quarterly inflows of INR 2,806 crores. Growth in deposits is in line with our guidance of reducing the CD ratio and bringing it closer to 80%, in line with the rest of the banking industry. Our retail deposits grew 15% sequentially and CASA grew 10% sequentially in a market where most banks are witnessing negative CASA growth. I believe this underlines our efforts towards building a granular liability franchise.

On the asset quality, our collection efficiency continues to be around 100%, taking our PAR further down to 4.9% from 6.1% as of September ’22. If you look for year-on-year improvement, it is around 1,000 basis points. As of December ’22, our GNPA is at 3.4% and NNPA is just 0.05%. Also, our SMA book, as well as restructured book have shrunk further indicating the reduced stress. The restructured book is now just INR 302 crores with collections, almost in line with the overall book.

On profitability side, our pre-provision operating profits stands at INR 389 crores with a PAT of INR 293 crores. NIM for the second — for this quarter was 9.4%. For the nine month period, our pre-provision operating profit stands at INR 1,074 crores with the profit-after-tax of INR 790 crores with the net interest margin of 9.6%. We expect Q4 ’23 to be similar to Q3 ’23.

Now an update on the merger with UFSL. As per the update published by SEBI on their website, basis our submission of scheme documents with the exchanges, the NOCs have been received from both the BSE and NSE on January 6th, and SEBI is in the process of seeking clarification from other regulatory bodies.

Further, Reserve Bank of India has given us notice to our application, which was uploaded on the exchanges last night. Once we are in receipt of the SEBI clearance, we will proceed to file the application with the NCLT. On submission of our application with the NCLT on receipt of their requisite regulatory and shareholder’s approval, we will positively expect to get the proposal — the proposed merger completed by September this year.

Now just a little bit on the outlook for the year ahead and for the fourth quarter. Going ahead, we will be growing our presence, both physically and digitally. In Q3, we added eight branches, marking our foray into the new state Telangana. As of today, we have 606 branches, in fact, 607, we have just opened one this — today. And are looking to add more this quarter.

Financial year ’24 branch addition would be close to between 50 and 70. Focus is to expand in deposit-rich catchment areas. In addition, as we have always maintained, we would look to add multiple connect points with our customers using technology as an enabler. Our digital initiatives are towards direct acquisition of liability and asset customers, FinTech partnerships, focus on our IBMB platform to generate more business.

Our Hello Ujjivan mobile app is the step in that direction. This has already had 60,000 downloads within a month. With this app, we wish to increase digital penetration among our mass market customers and inculcate banking habits. Also we wish to capitalize this asset to disburse MFI loans with very limited human intervention and focus on digital collections as well.

The process will be tedious and gradual, but has high potential of benefits, like improved collection, productivity, and reduced opex. We also look forward to automate the processes and use RPAs to improve productivity and service quality. With our digital taking shape, we are also working on shifting customers to cashless alternatives. During FY ’23, we have invested on our digital capabilities like video banking, KYC, access management and others. These would also help us in our digital journey.

Micro banking continues to be well backed by strong credit demand, while we did see some hiccups in process due to implementation of the new MFI credit norms, but that is all settled down now and we are seeing good disbursements. We continue to invest in the business and look to newer avenues like QR code, cashless collection, BC partnerships, and others.

The micro and small enterprises, we are currently in a transition phase and investing and expanding our product suites and services to be more relevant to the semi-formal and formal segment. Also, we are upgrading our technology platform to serve the customers better.

The other businesses that we have, one is housing. We are pleased to say that we have crossed the INR 3,000 crore OSP this year for housing. Incrementally, we are focusing on semi-formal in Tier 2 and Tier 3 towns. We implemented a state-wise collection collateral policy and ROI metrics and recently — and increased productivity. Consequently, the business has turned profitable. And we have now opened a couple of new asset centers as well, where housing will be operating out of these centers.

Vehicle finance, our IT integration is in place. We look to scale up the business in the coming year, once this is fully operational. Currently, we are doing limited business, majorly with ETB MFI customers. Now we are looking to focus on the new to bank customers as well. Among other secured businesses, we are looking to scale up our gold loan business once the test marketing is completed and this will be done commercially across 50+ branches.

Also our NBFC lending business is doing well with Nil delinquencies. We are focusing on our fee income with the addition of new products like 3 in 1 account, NPS and mutual fund in FY ’24. We are confident that the new initiatives will start materializing in the second half of ’24 one by one and you will see this impact.

Overall, we expect to grow our gross loan book by about 25% in FY ’24. Given the increase in cost of funds, there would be some pressure on NIMs, which we would need to manage by focusing on increased CASA, especially the CA part of it through yield expansion. While we would continue to invest in the tech and digital platforms, as well as brand visibility, we would keep cost-to-income ratio under control. FY ’23 has been an abnormal year in terms of credit cost, abnormal, what I mean is very good year in terms of credit costs.

Next year we expect provisions to move up towards 1% on average gross loan book and recoveries though significant, this would be lower than financial year '23. We would be able to share more details once we are — once we close the financial year. Dynamic, macroeconomic and geopolitical factors, along with inflation and rate scenario would be key monitorable items. However, given our business model and investment in various banking platforms, we are confident of a strong Q4 and a good fiscal 2024.

I'd like to stop here and request the operator to begin with Q&A. Thank you.

Moderator: First question is from the line of Renish Hareshbhai Bhuva from ICICI Securities. Please go ahead.

Renish Hareshbhai Bhuva: Yes. Hi, sir. And congrats on a great set of numbers. So sir, just two questions. One, on the deposit side, though the absolute deposit acquisition has been robust in the quarter. But when we look at the customer acquisition run-rate, which is roughly around INR 3 lakhs per quarter. So that had actually declined this quarter. So can you please throw some light on what is happening there in terms of the customer acquisition? Is there any particular channel, let's say, a digital or any particular geography which is, you know, under pressure which is leading to the lower customer acquisition?

Carol Furtado: Hi, this is Carol. Thank you for your question. So what we are doing currently is that we are focusing a lot more on the quality acquisition, than over quantity and increasing the acquisition of higher ATS customers. And that's the reason why you see a slight dip there. But this is just a one off and we will be increasing our customer acquisition.

Renish Hareshbhai Bhuva: Got it. Got it. Thank you on that. So my second question is on the opex strategy side. So if we look at the last three, four quarters trend in terms of the AUM mix — the share of MFI has been going up steadily, which is in contrast to what we have been stated since our SFB journey of our asset mix. So sir, what would be the strategy going into '24, '25 in terms of the AUM mix?

Ittira Davis: Yes. I mean, that's a good question. I think we have outlined our longer-term strategy which is to build a balanced 50-50 between secured and unsecured. As I just mentioned, we are developing several of our secured products, which will be launched into the market next year, that will help us. And we are also growing our secured housing and MSE portfolios. There are some system changes, which are taking place right now, which will help us to grow these portfolios faster.

So in the short-run, what has happened is that, post-COVID, we were more prepared with the micro-banking business as an overall to — to come out of COVID. So that is why it has grown faster. But eventually, the other businesses, the secured portfolios will have to catch-up and overtake in terms of rate of growth, but micro-banking will continue to be an important part of our portfolio. And as I said, eventually, in five years or thereabouts, we are looking at a 50-50 breakup between secured and unsecured debts.

Deepak Khetan: Also Renish, in the interim, as Mr. Davis mentioned, that the micro-banking portfolio is doing much better. We also need to see that the micro-banking portfolio is much more profitable also and giving us that kind of income that is required for the business to invest in all other businesses that we have.

Renish Hareshbhai Bhuva: Got it. Sir, just a last follow-up on the deposit side. What is the deposit rate hike we have taken, let's say, during the last three, four months?

Deepak Khetan: Come again, Renish. Which rate hike are you talking about?

Renish Hareshbhai Bhuva: Deposit rates, TD rates.

Martin Pampilly: So we have not taken any TD rate hike after November. The last we took was November and after that market has seen a decent amount of rate hike and we have not been taking rate hikes. We are still seeing very good flow on our liquidity side, our deposit intake, we just mentioned, Mr. Davis mentioned in his speech also, this quarter was very good in terms of overall deposit inflow. In fact, we got INR 2,800 crore of deposit inflow. And in January too, we saw very good amount of deposit inflow. So we haven't taken rate hike. And as of now, we are feeling — we feel comfortable with that…

Renish Hareshbhai Bhuva: So despite not picking the rate hike, we are seeing the incremental flows to be much higher. Fantastic. Thank you. Thank you.

Ittira Davis: We took the rate hike in November, but we are happy with that hike. We're not chasing to look at anymore hikes in the near-term. So we will watch the market. But what we did in November was adequate for us.

Renish Hareshbhai Bhuva: Got it. Because, in December, January actually the rate hike gathered pace. So just one thing we have not yet taken that rate hike, despite that we are able to garner before deposits. Okay.

Deepak Khetan: Yes, we have not participated in that change of December, January. So whatever we did in November has helped us get the deposit rate going — deposit garnering going.

Renish Hareshbhai Bhuva: Got it. Got it. That's it.

Moderator: The next question is from the line of Shreepal Doshi from Equirus.

Shreepal Doshi: Hello, sir. Good evening and thank you for giving me the opportunity, and congrats for the good set of numbers. Sir, the first question was for the micro individual loan category. So wanted to understand, when do we, is it only focus towards captive customers, captive GLG customers? And secondly, after how many cycles of being in the GLG cycle do we shift the GLG customer to individual category?

Vibhas Chandra: So, hi, thank you for the question. Individual loan is something which is we offer to our customers after completion of one GL cycle, but largely, we have seen that customers opt for individual lending generally after two or three cycles. This is answer to your first question. Second is?

Shreepal Doshi: 90%.

Ashish Goel: Yes. 90% of our customers in individual loans are the one who graduates from the home loans.

Carol Furtado: Yes, its existing customers.

Ashish Goel: Existing customers, largely they are existing customers.

Vibhas Chandra: So yes, we have put up for both the active customers, as well as open-market customer acquisition. But we have — largely focus on our internal customers as we have a large customer base. So more than — close to 95% customer acquisition happens through graduation of GL customers.

Shreepal Doshi: Okay. Got it. And sir, how is the process for this, like the disbursements and collections for this happens through the same channel or do we have a separate — like separate channel or separate channel for this particular business?

Vibhas Chandra: So yes, the entire acquisition process for GL lending. GL lending is something which is very old in Ujjivan. We have been doing GL lending business for last about 12 years. And process is — the product and process is that, as far as Ujjivan is concerned. The entire acquisition process and collection process is separate from group loan business. The customers who graduate to IL, the underwriting mechanism is very, very different which is they are in group loan. And apart from that, we have completely independent credit team right from the field to the top, which is — which has no relation with the business team and a great team besides upon ticket size and customer acquisition of GL lending customers.

As for our repayment concern, we offer different mediums and different channels for repayment, including UPI payment, SI payment, ACS payment and all other digital mediums which is possible for our customers to use. Apart from that, they can also — they are also welcome to center meetings as well as branches for repayment.

Shreepal Doshi: But, sir, here the model will be monthly, right? They will be paying monthly EMI sort of a model, right?

Vibhas Chandra: We offer frequencies but generally, we have seen both in group loan as well as individual lending customers generally opt for monthly as it is convenient.

Shreepal Doshi: Got it. So the second question was with respect to MFI book only. So after — once a customer has defaulted and we've written him off from the book, how much of the cooling time do we give to the customer that we can again sort of bring him on board? Or so do we have a strategy there or do we have a line of action there? Once we have written off a customer, can we again onboard him after six months or 12 months of a time period?

Ashish Goel: Shreepal, we have consciously not taken on board any customers who we have written off in the past. They are not in the qualifying list for acquisition.

Shreepal Doshi: Even if it has been written off by somebody else, so even in that case, we don't onboard such a customer.

Ashish Goel: Yes.

Shreepal Doshi: Got it, sir. Got it. Sir, the third question was we acquired 2.3 lakh new customers during this quarter. So what percentage of them were new to credit customer for us?

Ashish Goel: Approximately, 60:40. 60% are customers who had tracks with the industry, and about 40% turned into credit.

Shreepal Doshi: Okay. And, sir, during this quarter, disbursements, so in the MFI piece, what were to the existing customers and what were to the new customers? Like what percentage?

Ashish Goel: So about 35% to 40% is disbursements to new customers, the NCA, and between 65% to 70% are existing Ujjivan customers.

Shreepal Doshi: Got it, sir. The last question was if you could give details of the movement of NPA, that is what was the gross slippage, recoveries, upgrades? Write-off you've already given in your filing.

Ashish Goel: So on upgrade for the quarter, it was about INR 97 crores, which is about 10% of the gross NPA that we were having. And these slippages was about 0.5%.

Shreepal Doshi: Okay. Got it, sir. Thank you, sir, and good luck for the next quarters, sir. I'll come in the queue if I have more questions. Thank you.

Moderator: The next question is from the line of Gautam Jain from Gcj Financial Advisors. Please go ahead.

Gautam Jain: Good evening, sir.

Deepak Khetan: Good evening.

Gautam Jain: Yes. My first question pertains to your cashless collection, which is rising every quarter. So can you throw some light on it? What is it leading to such a high or increase in cashless collection? And what — any target we have in mind that we can reach to that level, just your thought on that?

Vibhas Chandra: Yes. So it all started during pandemic. Before pandemic also we were trying, but pandemic was a time when even customers started to learn. And we also learned that we have to provide different channels of repayment as during pandemic even we were not able to move into the field and for the collection. So during pandemic we developed various channels, digital channels through which customers can repay their EMI. And so take example of all the wallets, UPI payment, SI and ACH. These all models we established during pandemic and customers also adapted, and we saw a huge jump in cashless repayment from the customers. Looking at the success, we have also developed a mobile application, especially dedicated for micro-banking customer segment, which we call Hello Ujjivan, where customers can use it conveniently to repay our EMI and do many other things as far as banking is concerned.

So today, about 26% customers pay us digitally. This not only is convenient for our customers, but at the same time, it reduces your opex as well. As far as long-term numbers are concerned, we are looking at first looking at the milestone of 30%, but the data which is available in the market, that says that close to 40% to 45% customers at this point of time have smartphones, and we are targeting these customers in the next financial year, and this number will gradually increase. So we are looking at gathering more and more customers into a digital repayment so that the entire process of collection becomes much more inexpensive.

Gautam Jain: And which channel they use the most? I mean, Google Pay, G-Pay, or I mean.

Vibhas Chandra: It is — UPI is first, and followed by SI and ACH.

Gautam Jain: Okay. And my second question is, Mr. Davis has talked about the FY '24 to be a good year and credit cost to be around 1%. Can you also guide about what growth we would like to have in 2024 and what kind of cost-to-income ratio we want to achieve next year?

Deepak Khetan: Gautam Bhai, we'll come to that when we — as Mr. Davis mentioned, towards the close of the fiscal. Right now we can say that the broad growth guidance will be 25% and credit cost would be around 1% and we will keep a good tab on the cost-to-income ratio. This year, nine months is around 55%. Probably, we will be around that range only when we close the year, more or less. We will keep a very strong tab on the cost-to-income ratio. We will not want that to go up from where it is.

Moderator: Thank you, Mr. Jain. May we request that you return to the question queue for follow-up questions. We'll take the next question from the line of Shailesh Kanani from Centrum Broking.

Shailesh Kanani: Congratulations, sir on a good set of numbers, and thanks for the opportunity. Sir, my question is respect to comparative landscape on the industry side. Are we facing any competition or are there any pressure on yields?

Deepak Khetan: Overall, see, for industry-wide, there is a lot of banks, what we are seeing is there's a lot of pass-on that most of the banks are doing in terms of the interest rate hike. In fact, we have not been doing that, for example, in micro-banking, while peers have passed on a lot of rate hike, we have only taken a 50 bps rate hike so far. Even in housing, like Mr. Davis mentioned, it is linked to EBLR, the increased rate that we have done for the new disbursement is around 90 to 100 bps. We have not passed on yet. So we still have that up our sleeve that we will be able to do a little bit of a rate hike, and that's what he mentioned in his speech also that for whatever cost of fund hike is there, we'll have to see how we increase our yields going ahead.

Shailesh Kanani: We are not passing on as of now. But…

Deepak Khetan: As of now we're pretty comfortable where we are, and we see that as a buffer in our hand.

Carol Furtado: We are closely monitoring the situation, and we will take the calls at the right time because right now, we are in a comfortable situation.

Shailesh Kanani: *********

Moderator: Your audio is breaking from your line, sir. Please repeat your question.

Shailesh Kanani: So I was asking the same thing on TD rates. On deposit side as we are seeing good growth, I'm not seeing any pressure on that as well, right?

Carol Furtado: Not at the moment. We are able to hold onto to the rates.

Shailesh Kanani: Okay, sir. And sir, one last question. We are entering into new geographies. So can you just outline some strategy on that? Or how we approach to a new state, the credit culture over there and what is our basic premise of entering into a new state?

Carol Furtado: Okay. So we recently entered Telangana and we went ahead with the liabilities front. Our branches are more into retail liabilities. We will also be setting up the housing and the MSE teams out there. We are seeing a very good garnering of deposits happening in Telangana. We've opened four branches at the moment.

Moderator: Thank you. Mr. Kanani, may we request that you return to the question queue for follow-up questions. The next question is from the line of Sharaj from Laburnum Capital. Please go ahead.

Sharaj: Hello, sir. Thanks for the opportunity. My question is on the MSE lending side. What is the new strategy? We've tried this a couple of times, but we're not even successful. So what is the right to do-- and what are we targeting?

Carol Furtado: So on the MSE side, yes, I mean, we did speak about revising our strategy. We will be focusing a lot on the shorter tenure products in the strategy, going-forward and also our customer segment will move towards the semi formal and the formal segment. So this is something that we're working on. And also we have launched the product called Prime LAP for our customer segments for the longer-term loans. And this would be facilitated also to a large extent through our growth in FinTech partnerships.

Sharaj: So what would be a right to win here is what I'm trying to understand. Essentially, I mean, it's a new customer segment we're going after, new market entirely. So like, what is it that we'll be able — what is it that makes you think like we'll be able to succeed here? Like, what is it that we'll be doing differently?

Carol Furtado: I didn't get your question.

Deepak Khetan: Sorry, could you just repeat? It was not clear

Sharaj: Yes, sorry. The entire market segment, as in the customer profile, the businesses all will be different now, right? So what is it that will give us our edge here to succeed?

Carol Furtado: So we have always been in the semiformal segment, but we are going to focus a lot more in the semiformal segment. We have moved out of the informal segment. Our USP would continue to be customer service and technology would play a very important role for these customers.

Sharaj: Okay. And in the ticket side, you mentioned this time for the MSE lending, it's gone up from INR 20 lakhs to INR 40 lakhs and MSE fintech lending. So what is the difference here?

Deepak Khetan: So the fintech lending was short-term build discounting accounting kind of a product where the ticket sizes were very small and the tenors were also very short. So since we have discontinued that product for the time being, the difference is that our core lending book, the ticket sizes have not moved up significantly.

Moderator: Thank you, Mr. Sharaj. May we request that you return to the question queue for follow-up questions. The next question is from the line of Deepak Thakran from 1729 Advisors. Please go ahead. Mr. Thakran, your line is in talk mode. Please go ahead with your question. Mr. Thakran, please unmute your line from your side if muted. As there is no response from the current participant, we'll move onto the next question from the line of Ashlesh Sonje from Kotak Securities. Please go ahead.

Ashlesh Sonje: Hi team, congratulations. A couple of questions from my side. Firstly, on the deposit front, we have seen quite robust growth there, both on the savings accounts as well as retail term deposits. And I believe that TD rate has been increased by only about 40 basis points since September. So what exactly has worked for us in terms of our strategy to garner deposits here? If you can elaborate on that, please?

Carol Furtado: So I think what has worked for us is, of course, the interest rates, but I think this has also been supplemented with our customer service where we have been able to provide relationship banking services to our customers, getting a lot more granular. And also, we have seen the digital working well for us. We have also introduced the cash management, QR. And we have taken on a lot of efforts to increase the marketing activities in the local areas of our branches. And we have done two major all India marketing activities on newspapers, press, TV that has got us a lot of customer leads. And on the other side, we have also worked a lot on increasing the productivity of our staff. And this has also — again, we have done very thorough workshops with our branch managers and training to our sales teams. All these, put together, I guess, has increased the deposit base.

Ittira Davis: You might have seen us also in the New Zealand match yesterday, our advertising. We were all over the place. So branding has become very important.

Ashlesh Sonje: Okay. good to know, sir. Sir, would you say we would have added more to the sales staff on the liability side during the quarter?

Carol Furtado: We've not increased our sales staff.

Ashlesh Sonje: Okay.

Deepak Khetan: If you see, our overall employee count has not gone up significantly. So not much of addition has been there.

Carol Furtado: In fact, it has gone down.

Ashlesh Sonje: Perfect. Thanks, mam. The second question is on the.

Deepak Khetan: See, I think we would be adding a bit now with the new branches and even in the existing branches, we have identified few branches, which has much larger potential. So there we would be adding, and you will see the benefit of that coming in.

Ashlesh Sonje: Okay, thanks, Deepak. And secondly, on the individual loan book within MFI. Can you talk about the range of ticket sizes that we offer and the tenors offered in that segment?

Vibhas Chandra: So our range is INR 51,000 to INR 3 lakh, and it depends upon how many cycles customers are with us in GL and then IL as well. As far as their average ticket size is concerned, all the customers that we have lent, it is close to INR 1.2 lakh. And these are the two questions you had?

Ashlesh Sonje: Tenor?

Ittira Davis: Because we are now moving, we also offer customers tenure of two to three years as well, which is maximum. Our average tenor is close to 26 months.

Ashlesh Sonje: Okay. Perfect. Sir, if I may just squeeze in one last question on the slippages front. Can you clarify what the actual slippage number was in rupee terms and what is the way for accounting slippages? So let's say, a loan slips into NPA in the month of October but recovers in the same quarter, let's say, in the month of November. Would that be counted as a slippage the way you report it?

Ashish Goel: So our overall slippage number was INR 110 crores, these were net slippages. So there is an upgrade also which gets reported in the same quarter. So slippages and upgrades are netted off. So overall, I would say that the net slippage was about INR 14 crores for the quarter.

Moderator: The next question is from the line of Deepak Poddar from Sapphire Capital. Please go ahead.

Deepak Poddar: Yes. Hello, sir. Congratulations on a good set of numbers, sir. Sir, just wanted to understand — just one question I have. So in terms of rate hike, you mentioned, since November, we have not done any kind of rate hike, right? And this last cycle, we have not participated, right? So any plans for further rate hike that might be on the cards? So any thought process would be helpful.

Carol Furtado: Not at the moment, but then we are closely watching the situation, and we will take the call as and when it is required.

Deepak Poddar: Because you did say that next year, we are expecting some pressure on NIMs, right? So.

Ittira Davis: I just want to add. See the thing is that when we did make the rate hike, we did a good rate hike that we didn't have to keep adjusting 20, 30 basis points here and there. So we realized the cycle in which or the rate at which the markets and interest rates were moving, and we took a bold step in November, and we have held on to that.

Now going forward, if the Central Bank or the Reserve Bank of India continues to increase rates, then we have to watch that very carefully. So we are watching and we will do what it requires to keep us in the forefront of the deposit growth. So NIMs — yes, when NIMs are being squeezed, we also have to look at the lending side. And as I said, there is a potential that if the RBI raises interest rates, we may look at having to raise the lending rates as well because the lending rates on the micro-banking book, we have raised only once since September by 50 basis points, and we have not done anything else after that. So we have an opportunity to see if the rates go up and continue to go up, we may have to raise the lending rates as well.

Deepak Poddar: And in terms of pressure on NIMs, so what sort of basis point would be comfortable with? I mean, in terms of NIMs compression, if at all next year we can see. I mean, 20, 25 basis point, would that be comfortable for us to kind of absorb and not go for the rate hike?

Deepak Khetan: Deepak we will talk about more financial data about next year when we come back in the fourth quarter. Also, one more thing I'd like to add on the rate hike on the TD side. Our liquidity currently is quite good and we believe we are quite well placed for this quarter disbursement, even for the fourth quarter, which is generally expected to be a little higher compared to the other quarters. So we'll see how and what kind of rate hike is required.

Moderator: Thank you, Mr. Poddar. May we request that you return to the question queue for follow-up questions. The next question is from the line of Deepak Thakran from 1729 Advisors. Please go ahead. Mr. Deepak Thakran, your line is in.

Sanjay Pandit: Hello, can you hear me?

Ittira Davis: Yes, Deepak. Hi.

Sanjay Pandit: This is Sanjay Pandit here from 1729. Just a quick question. What is your run rate long-term.

Moderator: Your audio is breaking from your line. Please check.

Sanjay Pandit: Sorry. I have one question. What is your long-term return on assets and return on equity estimate/target as you look at your business across cycle? And the second question is by when do you think the reverse merger with Ujjivan Financial will be completed?

Deepak Khetan: Deepak on the longer term sustainable ROA is that what you are asking for, we believe. In this kind of a business is 2.25% to 2.5% kind of a sustainable ROA is easily manageable. And yes, and with a few years being exceptional like current year was a good year for us as an exception. So we are having that 4% kind of a return. And ROE is largely a factor of your what kind of capital adequacy you are maintaining.

So, given this year was a very — this year is after a rough patch, so we are maintaining a high capital adequacy, this wouldn't be the case. So our ROEs will accordingly adjust as the capital adequacy move. Industry-wise, I think capital adequacy for SFBs is around 20% — 20% to 22%. On your reverse merger question, we have mentioned in our press release also, and Mr. Davis covered in his speech also that we are awaiting a SEBI approval on the application that we have made, and then we will move to NCLT. With all the other regulatory approvals and all, we expect the process to close by September '23.

Sanjay Pandit: Thank you very much. Congrats on a good quarter.

Deepak Khetan: Thank you, Deepak.

Moderator: The next question is from the line of Bhuvnesh Garg from Investec Capital.

Bhuvnesh Garg: Yes. Hi, sir. Thank you for the opportunity. Sir, I would like to know what would be the number of active customers in group loans? And how it has moved in last three, four quarters?

Deepak Khetan: So our active micro-banking customers which I have off-hand is around 34 lakhs and it is up 25% YTD.

Bhuvnesh Garg: 25% YTD?

Deepak Khetan: Yes.

Bhuvnesh Garg: Okay. That's it from my side. Thank you, sir.

Deepak Khetan: Thank you.

Moderator: The next question is from the line of Yash Dantewadia from Dante Equity.

Yash Dantewadia: Hi, sir. Good evening. So my first question is regarding the floating provision. When are you planning to write back the amount to outlook? And what's the thought process behind this provision now? Because COVID is done I think. So I want to understand this first.

Ramesh Murthy: Hi, this is Ramesh Murthy here. Floating provision is governed by RBI norms. So it really depends on when the Reserve Bank of India allows us to take a call on floating provision. We have represented this matter to Reserve Bank of India and we are waiting for a response. So we have to just wait till RBI comes back to us, because this is under a regulatory guideline.

Yash Dantewadia: Okay. And my second question is, your H2 guidance was similar to H1 guidance, which was IINR 500 crore. Would you like to upgrade this guidance to maybe INR 600 crore now because of how the quarter 3 went?

Deepak Khetan: We just mentioned, Q4 would be more or less similar to Q3 in our speech, opening remarks.

Yash Dantewadia: So, your H2 guidance would be 600, right?

Ittira Davis: 600, yes, it is okay. And one more thing on the floating provision, it's good to have a little bit of floating provision, a little bit of extra cushion on your balance sheet.

Yash Dantewadia: Sir, my last question is regarding the secured and unsecured book ratio. You said you want to take it towards 50-50. By when do you see this happening?

Ittira Davis: Yes, we have a broad timeline for about five years. And within five years, we'd like to see this there. So from the next financial year, you will start seeing the unsecured book coming down a little bit at a time till it reaches 50-50. When I say five years, I'm talking about '28, '29 in that range.

Moderator: The next question is from the line of Ayush Vimal from Clearview Capital.

Ayush Vimal: Thanks for taking my question. Mr. Davis suggested that the share of secured book will actually go up from 28% to 50% over the next five, six years. I just wanted to understand the impact of this on the NIM over the long-term and the return on assets?

Ittira Davis: Yes. I mean, definitely the pricing on the secured book is lower than the micro-banking book. But we hope that the credit quality and other aspects will also enhance - the longer-term return on assets will be around the 2%, 2.5%, which is what we expect. And also the return-on-equity will have to be in line with what we are expecting from the market for this sort of thing. But the main thing is that, we build a balanced book and the risk is mitigated through this process.

Ayush Vimal: Thank you. And the next question I had was on the strategy that you'll be entering the gold loan segment sometime next year to shore up the secured book. Given that this segment is under intense competition at present, and there's lot of yield compression in banks entering the space, just wanted to understand the rationale for entering the segment at this point in time?

Vibhas Chandra: First thing is that we have entered into gold loan market. We have launched it in some branches, and we are testing, and we intend to start operation in about close to 50 branches next financial year. You are right that the competition is intense in gold loan, but at the same time, we see that in our micro-banking customers, the overlap is close to 10% to 11%, and that is a huge number. And we see that our customer is in demand of gold loans and because we are giving loan, we are also trying to offer them gold loans.

Apart from micro-banking loan, we have other customers also in the branches, including branch banking, MSE and housing, there also we see demand. And looking at the customer demand with an in-depth survey with the customers and even open market customers, we decided to enter into gold loan market business. And this will allow customers to take a one-stop-shop kind of solution where they can get all kind of loans that they need from us. At the same time, it will also help us increase our secured loan portfolio, which we target to reach 50-50 in the next five years.

Carol Furtado: And in addition, we will be launching this product in identified geographies, where we believe that it makes sense for us.

Moderator: Thank you, Mr. Vimal. May we request that you return to the question queue for follow-up questions. The next question is from the line of Sarvesh Gupta from Maximal Capitals.

Sarvesh Gupta: Sir, most of my queries are answered. Just one thing, like this quarter we had a Q-o-Q growth, but somehow the other expenses sort of made us not grow the pre-provision operating profit. So are there any one-offs related to the tech or some other initiatives that we have taken, which are expected to taper off in the coming quarters or this is business as usual?

Deepak Khetan: You are talking about other opex, right?

Sarvesh Gupta: Yes. I mean, you did grow your book on a quarter-to-quarter basis, but your pre-provision operating profit did not grow. So are there any one-offs related to the expenses also in the P&L, which are starting to sort of build-up?

Deepak Khetan: One thing that was there last quarter was a PSL income of around INR 14 crore, which is not there this quarter. PSL income doesn't come every quarter. It comes like in blocks when we sell the certificate and take that income. So last quarter, that income was there. This quarter, that income is not there. To some extent, the finance cost has gone up because of the rising interest rate as you have been listening on the call. Other opex, there have been a little bit of a marketing spend that we have done, a little bit of an investment that has gone in, for example, Mr. Davis mentioned in his speech also like one of the avenue on the micro-banking side is QR code, so little bit of investment has gone there. So all those investments, a little bit of branding and all that has put that other opex at INR 217 crore. Other than that, there is no one-off item in the other opex. But yes, on the income side, that income is not there versus Q-on-Q if you are comparing.

Sarvesh Gupta: And this long-term ROA sort of a thing that you're looking in the range of 2%, 2.5% seems to be pretty low compared to where we are already at 4.5-odd-percent because it would mean essentially that even if you are going to double your asset book in three years, perhaps with 25% growth, you will still be at the same level of profit after tax or something like that. So is that overly conservative guidance? Or what is leading to this sort of a number?

Deepak Khetan: So what we said as a sustainable ROA. The question was the sustainable ROA in this kind of a business. This year, as you are aware, the credit cost is almost negligible and the bad debt recoveries are quite high. That has increased or that has skewed the ROA this year towards on a higher side. But a long-term sustainable with all the changes that you're talking about, the ROAs sustainable should be around 2.5 percent.

Sarvesh Gupta: Understood. And what kind of cost-to-income that you are targeting? Any guidance on that?

Vibhas Chandra: We'll come with more details number — detailed numbers when we come towards the end of the quarter — end of the fiscal.

Moderator: Thank you. The next question is from the line of Vivek Gautam from GS Investments. Please go ahead.

Vivek Gautam: Yes, congratulations on good set of numbers, sir. Basically, [inaudible 0:53:54] after giving very good numbers post listing and somehow we when - the bad phase, our good performance was not the same. So besides, COVID, what were the factors which were there, and what have been the key learnings and how sustainable is our business now and any concern you still have, sir?

Deepak Khetan: We couldn't quite follow your question, there's a little bit of a background noise.

Vivek Gautam: Basically the question was that…

Moderator: Mr. Gautam, the audio is breaking from your line. Please check.

Vivek Gautam: Yes. Just wanted to understand the reasons behind the improved performance of late, and is it sustainable, particularly in view of the — we went through a bad patch post-COVID. COVID was one of the major reason. What were the other reasons, sir?

Ittira Davis: Yes, the bad patch which we went through in fiscal year '21, '22 was primarily due to COVID because we recognized many of our customers were affected by the COVID conditions, and we had to recognize and make provisions for that. So that was what we did and followed all the accounting and RBI guidelines on that front. Now that is behind us. We are turning around. And this year, we have had fantastic recoveries. Our collection team and our credit team have worked extensively with our customers. And what we are seeing is perhaps second to none in the industry, at least definitely in the small — SFB space.

So I think that is helping us. Now, this cannot — this is a very unique situation. And when we come to a more normal environment next financial year and beyond, the things will be different. And we'll be operating at a normal thing, not at current levels of profitability. It will come more normal profitability. But we expect the business to continue to do well and go back to what we were doing pre-COVID days in terms of how we were operating at that time. Our profitability was good, and the business was doing well. So I think when we get back to normal conditions, that is what we are aiming for.

Vivek Gautam: And, sir, one more thing, sir. In the current rising interest rate scenario, how will be our performance been and what can be the impact on the credit growth, sir?

Ittira Davis: Maybe the interest rate environment, so far we are not seeing a problem with loan growth. And that, I think, is not just us, the whole industry is continuing to see because we are coming out of COVID and there is a demand for credit. So I think that will continue into next year as well. Now if interest rates continue to remain high throughout next year, then we'll have to see how to address that situation. But the whole industry is expecting a turnaround or a decline in interest rate to start sometime in the second half of the financial year, definitely. So once that happens, I think the credit demand will continue to be sustained.

Moderator: Thank you. Ladies and gentlemen, we'll take the last question from the line of Tushar Sarda from Athena Investments. Please go ahead.

Tushar Sarda: Yes, thank you for the opportunity. I just wanted to understand your normalized profit. So you've got PPOP of INR 389 crores this year, which has INR 30 crores miscellaneous income or bad debt recovery, which I assume will not recur in a normal year, right? Right now, we have lot of NPA. So it may continue for a year or so. But after that, it will taper off. Is that assumption correct?

Ashish Goel: True, that's right. So bad debt recovery is something because we had a lot of bad debt accumulation last year. So recovery process and our investment into the collections infrastructure has given us some very good result this year. But over a period of next four to six quarters, obviously, this number is not going to sustain.

Tushar Sarda: And you allow credit costs coming in, we're guiding for 100 basis point on the gross number?

Ashish Goel: That's right. That is right.

Tushar Sarda: And what would be the tax-rate, one should assume 25%?

Deepak Khetan: Yes.

Tushar Sarda: That's it from my side. Thank you very much and congratulations on a superb set of performance.

Moderator: Thank you. Ladies and gentlemen, that was the last question for today. I now hand the conference over to the management for closing comments.

Ittira Davis: Well, thank you very much. I appreciate the time all of you have taken to join us and participate in this discussion and conference. I'd like to thank our partners IIFL for organizing this, and appreciate the support that they've given us. Thank you very much and have a good evening.

Moderator: Ladies and gentlemen on behalf of IIFL Securities Limited, that concludes this conference. Thank you for joining us and you may disconnect your lines.