“Arman Financial Services Limited

Q2 FY '23 Earnings Conference Call”

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MODERATOR: **MR. JIGNESH SHIAL – INCRED EQUITIES**

Moderator: Ladies and gentlemen, good day, and welcome to Arman Financial Services Limited 2Q and H1 FY '23 Earnings Conference Call hosted by InCred Equities. As a reminder, all participant lines will be in 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. Jignesh Shial from InCred Equities. Thank you, and over to you, sir.

Jignesh Shial: Yes. Thank you, Aman, and good evening, everyone. On behalf of InCred Equities, I welcome you all to Arman Financial Services Limited 2Q and H1 FY '23 earnings conference call. We have along with us Mr. Jayendra Bhai Patel, Vice Chairman and Managing Director; Mr. Aalok Patel, Joint Managing Director; and Mr. Vivek Modi, Group CFO.

We are thankful to the management for allowing us this opportunity. I would now like to hand it over to Mr. Jayendra Bhai Patel, Vice Chairman and Managing Director of Arman Financial Services Limited for his opening remarks. Over to you, sir.

Jayendra Patel: Thank you, Jignesh. On behalf of Arman Financial Services Limited, I extend a warm welcome to our Q2 and H1 FY '23 earnings conference call. With me, I have Aalok Patel, Joint Managing Director; and Vivek Modi, Group CFO. We have also on the call representatives from SGA, the Investor Relations team. I hope everyone has an opportunity to go through the results and presentation for the quarter and half year ended September 30, 2022, which was uploaded on the stock exchanges and the company website.

In the past two years, Microfinance sector has successfully navigated this pandemic and is back on the track showing healthy demand. Additionally, the Reserve Bank of India's new guidelines is expected to help the industry grow even faster. During the H1 FY '23, the industry was focused on adopting these new norms on account of which the loan disbursement slightly subdued. However, the Microfinance business has emerged as one of the important tools for promoting financial inclusion and serves as the last mile of credit to those at bottom of the pyramid.

And at Arman, we are focused on servicing the low-income, underserved regions of the nation, promoting livelihoods and offering micro credit to socioeconomically backward people who have little to no access to the formal banking or financial services system. At present, we have a presence in 8 states with comprehensive branch network of 313 and a workforce of 2,620.

Of all the states, Gujarat contributes 31.9% to our AUM on a consolidated basis, followed by Uttar Pradesh, Maharashtra and Rajasthan. Company has recently forayed in two new states of Bihar and Haryana. We will continue to focus on extending our presence in newer districts in existing states, while also exploring new states.

On a consolidated basis, gross NPA stood at 3.3% and net NPA stood at 0.1%, showing an improvement of 230 bps and 100 bps, respectively, on account of improvements in collection efforts and lower provisioning. Cumulative provision stood at INR 70 crores, that is 4.9% of the consolidated AUM and 5.2% on book POS portfolio outstanding.

Therefore, total provisions remained much higher than GNPA. Collection efficiency improved to 98.3% in October 2022 as compared to 95.3% in March 2022. Collection efficiency across all segments has shown improvement and aligned with the pre-COVID levels. This was mainly due to the passionate on-ground workforce, continuous customer interactions and a customer-focused approach.

Collection efficiency for October 2022 for various segments stood as follows: Microfinance segment, 98.4%; MSME segments, 98.1%; two-wheeler collection, 96.7%. Now coming to the borrowing profile and liquidity. As on 30th September 2022, company has total borrowings worth INR 1,419 crores. Of the total borrowings, 53.8% is through banks and NBFCs, 21.7% is through securitization and PTC route and 14.1% is through NCDs and the rest is borrowed through DFIs, ECBs and direct assignments.

I'm happy to share that during the quarter, the company successfully raised INR 115 crores via allotment of CCDs and OCRPS on a preferential basis. The arrangement stand as follows: company has allotted 6,24,388 unsecured compulsory convertible debentures or what you call CCDs amounting to INR 77 crores. Some of the marquee investors include fund or funds controlled by Singapore-based Sixteenth Street Capital and USA-based Seven Canyons Advisors.

Other investors include both domestic and foreign individuals. Company has also allotted 3,10,972 optionally convertible redeemable preference shares or you can call them, OCRPS amounting to INR 38 crores. These were allotted to individual investors and family offices. The mix of Tier 1 and 2 equity capital will be used to fund the targeted growth plans of approximately INR 2,500 crores with a healthy capital adequacy and a debt-equity ratio by leveraging our presence in the MFI, MSME, 2-wheeler and other loan segments, which will enable the company to achieve a sustainable growth momentum in the coming few quarters.

As per Ind AS, company is required to split hybrid instruments into debt and equity. And therefore, the company's balance sheet net worth stood at INR 311 crores. However, fully diluted net worth, assuming full conversion stands at INR 362 crores. Also, we have a healthy liquidity position with INR 376 crores in cash, bank balance, liquid investments and undrawn CC limits.

Capital adequacy for Arman on standalone basis stands at 51.21%, I repeat, 51.21% and for Namra, our subsidiary, stands at 20.51%. With the equity fund raised and new LOS LMS system, we will steer the next phase of our growth and expansion by harnessing the power of technology and innovations to create a smarter organization that will enhance customer experience. We will grow this business at a careful but steady pace by spreading out across states, building necessary capabilities and adding relevant resources.

With that, I would like to request the operator to open the floor for any questions-and-answers session. Thank you all so much for joining. Thank you.

Moderator: First question is from the line of Virat from Shah Investments.

Virat: Sir, what kind of AUM and disbursement growth are we targeting for FY '23? Any comments on this?

Aalok Patel: Comments on that, typically, we try to grow between 35% to 40% CAGR over the long run. So it will be somewhere in line with that. But on projected results for FY -- for next year.

Virat: Okay. And how do we plan to utilize the fundraise of INR 115 crores?

Aalok Patel: So as you know, in an NBFC, there are regulated ratios to maintain namely the capital adequacy ratio, and we were approaching close to that. And hence, was required for us to raise this excess capital. And the funds will be used just for onward lending and to leverage on top of that to increase our AUMs.

Moderator: The next question is from the line of Anjana from Shah Investments.

Anjana: A couple of questions from my end. So the first one, I would just want to know if you can throw some light on the reduction of our MFI book. So we plan to reduce our MFI booking some 60% of AUM. Could you elaborate on the same?

Aalok Patel: We plan to reduce our MFI book to 60% of group AUM. You're talking of this from something like 80% to the brought down to 60%. Are you trying to say that? No. I mean there is a long-term plan to diversify the product line into other ancillary products like micro enterprise that we have, which is about 14% of AUM. We have also individual business loans, which is 2%, 2-wheeler loans is 4%.

So the long-term goal is to get more into micro ancillary products rather than the JLG product, but we still very much plan to be in the micro retail segment serving the rural customers. But I think that is what you are referring to. Overall, as time goes on, I think more and more the Microfinance segment has been showing extremely good growth in the past 10 to 12 years.

And going forward, we expect it to continue growing at least for another 3 to 5 years. Post that, we expect that the other products such as micro enterprise and individual business loans will start showing more growth than the JLG based group loans. Now these are estimates, of course. The market forces will behave as they behave down the future, but that is our expectation.

Anjana: Sir, also, how do we see our 2-wheeler and MSME business panning out?

Aalok Patel: They are doing extreme well I mean, so we'll take one at a time. So MSME is doing extremely well. I think over COVID, it has performed really well. But it takes a very specific kind of customer. And if you're comparing like, let's say, a growth rate between group-based unsecured JLG lending versus the micro enterprise with much higher underwriting and everything, it's not very, very comparable. So the growth rates might be a little dwarfed by the rate of what Microfinance is growing. But still MSME stands on its own and is an extremely good and extremely compatible segment that we are running.

Now as far as 2-wheeler is concerned, that industry has been in the doldrums since COVID and even before that. I think if you look at the amount of vehicles sold in 2019 at somewhere around 21 million to somewhere around 13 million in the last 12 months. Overall, the volumes of 2-wheeler sales have declined drastically over the last 3-odd years. So we have not completely discounted 2-wheelers, it's hanging in there, but there are tough times in the past and probably tough times in the future as well for the 2-wheelers payment.

Anjana: Sir, we have started disbursing loans under IBL segment. How do we see this panning out in coming quarters?

Aalok Patel: So coming quarter, may be it's too early to tell. But in the coming couple of years, the idea is that a lot of these Microfinance customers who have been with the company for several years, five to six years and have been Microfinance customers for 10 to 15 years even in many cases. Rightfully there is a requirement can we graduate them away from these group-based loans into individual loans.

And the natural progression and evolution also is to get away from cash-based collection into cashless collection. So that is the goal overall. And I think it will take a couple of years to gain good traction in this industry, but we are planting seeds right now as far as diversing away from pure JLG-based, group-based Microfinance.

Anjana: But then, sir, with these IBL loans, do we foresee any risk-based pricing model coming in play, which is not possible under JLG.

Aalok Patel: Risk in terms of what? You said pricing?

Anjana: Risk-based pricing model, basically.

Aalok Patel: No. I mean a lot of these customers have been with us and have some amazing track record even during COVID. So I consider these customers to be very, very safe. And let me also tell you that the repayment rate in this segment, although it's only 2% of the book. The repayment rate is 100%. We don't have INR 1 in overdue or default in this segment so far. It's a little early to celebrate. But we consider this as very low-risk customers. Vivek, you want to add anything?

Vivek Modi: Yes. So largely, at this stage, these are basically our own set of customers, who probably are dropping out of JLG and hence, it's about retaining the best-in-class customers with through product innovation. Over a longer period, since these would become kind of a full banking kind of customers, we might also kind of graduate over a period of time to a larger ticket size loans, which could be there. But those are like things in the future. At this point of time, it is more about retaining our quality customers with the IBL kind of thing.

Aalok Patel: Absolutely. So a lot of the studies that we were doing on our retention levels, we saw many of these customers kind of leaving after three or four cycles with us and the question was why. And the answer was that they were going for individual based loans from banks or SFBs. And these were our cream customers. So why should we lose them? We can service them just as well as any other bank.

Moderator: The next question is from the line of Savi Jain from 2Point2 Capital.

Savi Jain: Yes. And you mentioned that there were some liquidity challenges during the quarter. Has that normalized now this quarter?

Aalok Patel: Yes, yes. It's completely normalized. In fact, we are facing a reverse issue. I think largely speaking as we were approaching our CAR ratio, obviously, most banks do not wait for your debt equity or capital adequacy to go down to 15. So that was 1 challenge. Macroeconomics was another challenge. And frankly, we have not faced liquidity issues in our Company at least for the last 10, 12 years. But yes, for a month, 1.5 months, we did face some issues that has been largely solved that is to the recent fund raise. And it also gave us some time, fortunately to transfer and transition into our new LOS and LMS system. So all in all, we made good use of it as well.

Savi Jain: This CCDs and everything for the rating agencies do they consider that as equity or...

Aalok Patel: CCDs is considered as pure equity, it's a Tier 1 equity because it's compulsory convertible. In case of OCRPS, it's a Tier 2 equity until converted because its optionally convertible or you can redeem it as well. But yes, CCDs is considered as pure equity and OCRPS is Tier 2 equity. So it's like a hybrid debt.

Savi Jain: So they will at least lose the CCD -- they will include CCD for -- give the benefit of CCDs for rating and the numbers?

Aalok Patel: And some portion of OCRPS as well because there are multiple investors. And I think if you look at the balance sheet and as Jayendrabhai said in his speech also, under Ind AS, hybrid debt instruments have to be split between debt and equity. So the net worth you'll be seeing is around INR 311 crores, while fully diluted net worth, if you consider everything converting today would be INR 362, INR 363 crores or something like that. So already, there is a discount given because of the hybrid nature of these instruments in the net worth of the balance sheet under Ind AS itself.

Savi Jain: And the individual loan that you were talking about, is it the same in MSME? What is the difference there?

Aalok Patel: Similar, but the clientele is slightly different. So on one side, we are in the MSME side, we are finding cash customers, and it's a cash-based collection. On the individual business loan side, which are graduated Microfinance customers. So the underwriting might not be as stringent because we have three, four, five years of experience with them, but we have switched them to a cashless collection model.

So as I said, Savi, we are planting seeds. Yes, there are some similarities for sure between the products, especially as far as ticket sizes are concerned on average. But the sourcing is different, and the repayment or the collection methodology is different.

Savi Jain: In the MSME loans, which we are doing, is this similar to what 5-star is doing with lower ticket size is that the right way to look at it?

Aalok Patel: I'm not sure it actually does. 5-star's average ticket size is somewhere around INR 5 lakh, INR 6 lakh, if I'm not mistaken.

Savi Jain: They are lower. But yes, they are the only difference is they do secure. You do unsecured. Your yields are obviously higher than this, but is it a logical progression for you to move into higher ticket size and may be secured. Is that possible for you?

Aalok Patel: Yes, absolutely. It's worth considering. The models are different. And I don't know 5-star's model, but largely speaking, it's a secured asset which is difficult to repossess. So with the limited amount of research I've done into it. Of course, there is a sentimental value of having your residence or your house mortgaged. But in case of a default, very difficult to repossess these assets.

Savi Jain: That's true. Even Equitas says the same thing about the SBL customer. But I think the difference on the credit cost is simply for unsecured loan versus a secured loan, and even though it may not be technically possible to repossess. But I guess the credit costs are much lower just because of the fact that the kind of mortgage their house.

Aalok Patel: You are absolutely correct. And we have discussed this both at a Board level and individually as well. It might be something which is a natural progression for us, and let's see. I think certainly, I'm not discounting it as a viable division in the future.

Savi Jain: I think the only difference is that the GDP per capita in your state is much lower than the Southern states. And I think that makes it more difficult to do it in North or in the rest of the country as compared to south of India.

Aalok Patel: The difficulty also lies in the fact of the paperwork and the legal work involved, especially if you talk about the rural areas, primarily mortgaging in the rural areas at least is very difficult because the paperwork is very weak.

Savi Jain: Provisioning, with respect to COVID, is that over in this quarter, no?

Aalok Patel: Yes. Everything pre-COVID, which is assets disbursed prior to March 2020 is done and dusted, written-off or provided for it. So that's over with. Yes. So that's, yes.

Savi Jain: But the provision is still seeing a little high is it because you're providing the standard asset provisioning is seen.

Aalok Patel: The asset size has increased, the standard asset has increased and also the fact that Microfinance is no longer under the 1% loan loss regime. You'll have to expect a couple of percent. So we are monitoring that closely. And thanks to the RBI regulations also, to a certain extent, it has been passed on to the customers as well through margin increases and rate increases. But yes, I think a lot of it is related to pre-COVID NPAs as well.

Savi Jain: So what is the standard asset provision percentage that you're now using?

Aalok Patel: I mean we are under ECL provisioning. So our provisioning at 5.2% and NPA, 3.2%. So in a layman's term, you can call it 2%, if you like.

Savi Jain: On the standard assets?

Aalok Patel: On the standard assets.

Savi Jain: That's higher than what it was pre-COVID.

Vivek Modi: Yes, it is definitely higher than pre-COVID. Again, the reasons for it being slightly higher is also the fact that there are pre-COVID book, which were restructured and are in standard buckets continue to have a bit of higher provisioning, but they continue to be in standard buckets. So from that aspect, also there is there. And overall, the management overlay has been created during the COVID sales will be there for some time, till it kind of tapers off. And if we look at the entire ECL model based on the overall experience the last five years, and kind of we do the requirements.

Aalok Patel: I think as our auditor told us, there are no black swans in ECL, no black or no white swans, only history.

Savi Jain: So why is it that we have been, we released provisions in the standalone numbers?

Aalok Patel: Mostly write-backs. So a lot of these are write-backs in the standalone side.

Savi Jain: So growth number for this year? We have number for this year and next FY '24?

Aalok Patel: I mean, I wouldn't want to comment on the growth numbers this time but you have a better idea.

Moderator: The next question from the line of Srinath V. from Bellwether Capital.

Srinath V: Just want to find out from a NIM perspective, has the new regulation kind of fully kicked in, or do we need to wait for a couple of more quarters for the old book to kind of get flushed out and the old re-pricing? Are we likely to see some more NIM accretion over the next couple of quarters?

Aalok Patel: Yes. I don't know. So I think it will take a few more quarters. But Vivek, I don't have that number of what percent of the book is, new regime versus old regime, but it will be a significant weightage at this point.

Vivek Modi: So at this point of time, probably we don't have a specific number to share with you. But by a simple back of the palm kind of a calculation, at least 60% still continues to be old regime because we were at about INR 1,100 crores in Microfinance when the regime changed. And right now we are at INR 1,200 crores. So when you count INR 90-odd crores of prepayment. So by that logic, largely it will be 60%. But since the average balance tenure of the loans as on, say, March 2022 would have been approximately 15 to 18 months. So it will take some time where it kind of completely paid-off.

Aalok Patel: As far as your NIM question goes, see, our cost of borrowing has been going up significantly also since the last, because of the repo changes and stuff. So while we do expect NIMs to increase in the future, it will not be to such a large extent because it will be offset by some bit of absorption in the cost of borrowings.

Srinath V: **After IND AS**, the larger part of the NIM accretion has already taken place in the last two quarters. Fair understanding. Is that a fair understanding?

Aalok Patel: I would disagree with that. I would say about half of it is done, half of it remains.

Srinath V: Moving on just I want to understand how has been, have you faced any feeding issues in implementing the new regulation? Of course, we have a significant edge given that we already do all of this in MSME. But from what I remember, those set of employees are a grade or two higher when you hire them in first place. So are you facing, how is the on-ground situation on income assessment and documenting it and then kind of figuring out that I can't remember, again, 50% of there's some limit the government has given. So how is this whole process working on the ground? And how do you see that improving over the next six, eight months or one year or so?

Aalok Patel: No, it's definitely a work in progress. I think, overall, in April, we had used our old system and kind of done a best effort job of evaluating that is continuously improving, and it has improved significantly with our new software conversion as well as far as inputting all the right kinds of information to assess income. Besides that, I think since we are capturing household indebtedness as a result of that, rejection rates have also increased. And I think that message has been consistent with a lot of the other MFI players as well so all-in-all, I think is the rejection rate has slightly increased because of this.

Srinath V: Just pinching a last question before I go, just I want to find out if you've opened any new geographies, any new micro markets. And if we have made some progress on going into lower density areas because of the flexibility in pricing. And also, have you disaggregated pricing because we have had a very different credit cost experiences over the last couple of years in different micro market trends, even from Demonetization for today so are we looking at disaggregated yield structures in different markets based on your risk perception and so on?

Aalok Patel: So we have not done that yet. That is part of the plan in the long run, maybe starting from the fourth quarter or the first quarter the geographic based pricing or risk-based assessment pricing. Now as far as the micro markets are concerned, no, I think the past couple of quarters have been challenging with a lot of different projects in our hands with RBI implementation, with software implementation with liquidity, capital raise and stuff.

And obviously, the growth that we are looking at, which is ongoing. But yes, that is something to consider. I. think I can confidently more say about the differential pricing in geographies. As far as moving into these micro markets, you know we are never a first mover into any kind of a new situation. So that will be sort of slower.

Let us see what the competition is doing and what their experiences are in some of these markets. Other than that, we recently moved into Bihar, planning to expand on that in the coming few months. And Bihar has been behaving wonderfully. So that has been a pretty decent foray in to a different, into a new state.

Srinath V: It is running out of your Uttar Pradesh team itself or you now kind of have a completely new setup put in so on?

Aalok Patel: It will run out of UP team until Q4. After that, we'll split it from Q1 next year.

Moderator: Next question is the line of Yash Mandawewala from Mandawewala Family Office.

Yash Mandawewala: Congratulations on a good set of numbers. Aalok, we've just, most of the FMCG companies seem to be complaining about poor rural demand yet most Microfinance companies such as yourselves are reporting good collection efficiencies. So what is really happening on the ground? How is there this divergence of commentary on the same set of customers?

Aalok Patel: I mean, Yash, I don't consider myself an expert on macro or microeconomics. All I can say is that we have not faced so much of a difficulty or so much of a feedback from our operations or fields that people are facing any large-scale difficulties as far as economics are concerned or weak rural demand or everything is concerned. But maybe there is a lag effect, I don't know. But other than that, I wouldn't want to comment anything more on that.

Yash Mandawewala: Maybe let's wait and watch. Just one more on the new software system. So is the implementation now completely done? And I know it's early days, but where are you seeing sort of large differences? Where are you seeing significant value add from the new software?

Aalok Patel: No. So I mean, already, our PAT has reduced by about 30%, 40%. So that has been a big achievement. Overall, it was very successful and a lot of things had to go correctly. It is fully implemented now, and we are collecting large volumes of data. The risk controls have increased, skyrocketed overall with geo-tagging and everything. We are using digital signatures now. We have a tie up with legality, completely paperless. So it has a lot of different changes. And yes, I think overall, it has already been a big success.

Yash Mandawewala: Do you think in the end, it will lead to the loan officer being able to handle a higher volume of clients, customers?

Aalok Patel: It could, but I'm not exactly sure whether that should be the goal because higher per person capacity also comes with its own set of risks when something goes wrong. So when the delinquency and stuff rise, one person is not able to manage such a large case load. And the group sizes also have been overall in the industry going slightly lower as years go by. But what will help us in the future is moving more towards the cashless repayment. And in that case, yes, an FO will be able to handle more customers, but that will be a whole new model. Under the current model, I don't think that is our overall goal is to increase the case load for FO, although that might be an ancillary benefit down the road.

Moderator: Our next question is from the line of Balkrushna Vaghasia from Axanoun Investment Management.

Balkrushna Vaghasia: Many congratulations for the great quarter. So I want to know what is the average turnaround time, customer turnaround time for Microfinance and MSME business?

Aalok Patel: So for Microfinance, it goes state by state, I have the figures. I think it's approximately 4.6 days the last time checked.

Balkrushna Vaghasia: For Microfinance?

Vivek Modi: Three days is the customary or the regulatory training that we have.

Aalok Patel: So it cannot be less than three days. And the previous software, it was at least six to seven days. So we have brought it down to that much. In MSME, we have brought it down from 12 days to about eight days, but there is still a lot of room for improvement there.

Balkrushna Vaghasia: And what is the branch expansion plan for the second half?

Aalok Patel: So, the plan is to open about between 15 to 20 branches, for Q4, we are still working on that, so you'll have to wait on that question for the next quarter's con call.

Balkrushna Vaghasia: So 15 to 20 branches in Q3?

Aalok Patel: Correct.

Vivek Modi: More like for the FY '24, right. So normally, we've kind of seen a larger branch expansion happening in the first quarter, fourth quarter and the first quarter of the next year.

Aalok Patel: Exactly. So when we do our planning for FY '24, so a lot of the branch openings will happen in February, March, April, May time frame. But we don't expect a lot of business to come out of those in the current FY.

Balkrushna Vaghasia: So in terms of the average lending rate that before the new regulation and the after, I mean post the new regulation, what is the change in average lending rate in Microfinance that you are observed in your loan book?

Aalok Patel: About 2.5% has been the increase.

Balkrushna Vaghasia: 2.5%? And in terms of MSME segment, two, three years back when or maybe four years back when you started MSME segment, you say that, okay, I do the experiment initially, and then I'm satisfied about scalability of the particular business, then we go with full force. So like are you satisfied with the MSME segment and you want to go on full throttle on this, or what do you think, or do you want to scale this business now?

Aalok Patel: We are very satisfied with MSME, and it is no longer an experiment. It is definitely a full-blown division. But as I answered the first question, I'll kind of give you the same answer is that we are growing and we are growing well, but it requires the specific type of customer in the MSME.

The rejection rate is still about 70% in that division. So if you are going to compare apples-to-apples in terms of growth rate, for compared to micro and MSME, my lesson learned is it's not going to be very comparable. But we are still growing at good 20%, 25% of AUM.

Vivek Modi: On a Y-o-Y business, what happens is, obviously, FY '22 September, we had just come out of the second wave of COVID. But still, if we use September '21 as a benchmark for both Microfinance and MSME, I think MSME, again, in our case, has grown almost 60% from something like INR 125 crores as of September '21 to about almost INR 200 crores today, September '22. So I think MSME has been showing good growth generally, and can see good times going forward as well.

Balkrushna Vaghasia: And which segment among all of your like Microfinance, MSME, individual loan and vehicle finance, so which is the most profitable for you, including the effect of NPAs as well?

Aalok Patel: Definitely, if you compare just the bottom line margin, MSME is the most profitable, followed by Microfinance and followed by two-wheelers. But I mean, these are very, I don't want to say very different businesses. They are not very-very different businesses, but these are different businesses. On one hand, you have a better growth potential. On the other hand, you have a better margins. So we try to take the best of both worlds and do both the businesses.

Balkrushna Vaghasia: And last question. For Microfinance, how many of your customers are unique to you?

Aalok Patel: So that is, I always give a disclaimer to that question. Unique to me only applies to when I'm pulling the credit bureau report and I find it as no other financial institution where they have an active loan with. So that is approximately 25%. But after I loan them the money, if they borrow from somebody else, I have no track of that.

Balkrushna Vaghasia: And what is the cycle-wise classification of the borrowers like first cycle, second cycle in Microfinance?

Aalok Patel: Vivek, do you have that?

Aalok Patel: So about 65% is booked as first cycle. Rest of it is second cycle and above. Exact breakout, unfortunately, I'll have to pull it out right. I mean I have an idea, but I don't want to give you wrong numbers.

Moderator: The next question is from the line of Amit Mantri from 2point2 Capital.

Amit Mantri: So I just wanted to understand. So in the MFI book, what has been now the number on what percentage of the March 2020 book went bad? So on a static pool basis, what was the credit cost for the MFI book?

Aalok Patel: 10% to 12%.

Amit Mantri: Okay. And so basically post COVID, which is FY '21 and FY '22 disbursals, there, you didn't really have any significant credit cost, is it?

Aalok Patel: Not yet, but we are expecting somewhere around 2% on post-COVID on an ongoing basis.

Amit Mantri: And second question, now the book is almost close to INR 1,500 crores, and you eventually 1.5 years maybe look to get to INR 2,500 crores. So on the management side, management side, have there been any additions that you're making and plan to make going forward?

Aalok Patel: We had a CRO who joined, Mr. Raghavan, Chief Risk Officer. Other than that, I don't know, of course, a lot of team members joined, not on a C-level position other than Raghavan.

Vivek Modi: But yes, we are looking at in terms of an HR perspective, also kind of moving from the regional management system to maybe a zonal kind of a management where we kind of take the entire geographies that we work into various zones and kind of provide more bench strength in terms of the overall operations.

Moderator: The next question is from the line of Hirenkumar Desai, an individual investor.

Hirenkumar Desai: Yes, congratulation on a good set of numbers. The question is in this inflationary situation and one of the participants asked about FMCG sales being very low. And I mean, for some difficulty with that section of the society. So do we have a breakup of what portion of our loan is for business or livelihood earning or something like that? And what proportion of consumption?

Aalok Patel: So technically, all of our loans in Microfinance and MSME both are for income-generating activities, which is not to say that once you give the money whether some of it winds up to consumer. But largely speaking, all of our efforts is to make sure it's for some income-generating activity.

Hirenkumar Desai: And the second question is after the usage of the software and as we move forward, do we hope to see some operating leverage in terms of opex coming down as a percentage of assets or income whichever way you look at?

Aalok Patel: I mean, no. Sir, that is always a hope. And as Jayendrabhai would put it that cost-cutting and finding efficiency is always a constant endeavor. However, you will find us to be quite lean overall, how much extra lean that we can become, I think the idea is to always find a balance. If your goal is to become the leanest and the most cost-efficient company in the industry, you might get some good short-term results but that means is you are not investing enough. Your people might get frustrated. Your retention might suffer and a lot of other things might happen.

With the software, definitely, we are expecting to see efficiency of the FOs increase in terms of the number of disbursements they can make. And largely speaking, the second biggest goal was to reduce the overall risk in terms of operations and in terms of credit risk to the customer. So those were the large two goals with the software implementation.

Hirenkumar Desai: Last question, if I can sneak in is, while interest rates are rising, assuming that most of our customers borrow at a fairly high rate, how sensitive are we to the rate that we are charging? The question is in the rising rate environment, I mean, have you correlated to some past cycles or something like that to say, how it impacts our growth?

Aalok Patel: Surprisingly, sir, they are not at all sensitive to interest rates. And largely speaking they are able to absorb 1% or 2% here and there without any problem. And frankly speaking, not saying too much. Now any large-scale increases like 4%, 5%, obviously, it will be a problem. But generally speaking, for us, going from a weighted-average cost of borrowing of 11.5% to 13% would be a huge problem because the ROE will reduce by 1.5%. For them, it will make a difference of INR 20, INR 25 in their EMIs, which most people don't notice or don't care enough about. All they care about is timely availability of funds in the least hassle which causes them a least amount of disruption and hassles, if I can put it that way and a good level of service.

Moderator: The next question as the last question from the line of Savi Jain from 2Point2 Capital has a follow-up question.

Savi Jain: Yes. Where does this equity take you in terms how many years of growth can be taken care of by this equity raise?

Aalok Patel: That's the million-dollar question. You have your own internal accruals. So depends on what kind of ROE we can generate and depends on what kind of ROA and internal accruals that we can get. If we are growing at our rate of ROE, then we don't – we never need to raise. We can go indefinitely on our own internal accruals.

Savi Jain: Yes. I mean basically, this equity is just kind of the three years of growth and the leverage increase has been taken care of. And now, you are at a level where it's a comfortable car. So a 30% growth rate and 30% ROE, you would not need to raise any equity?

Aalok Patel: Exactly. Exactly. So I mean 30% ROE is difficult to maintain. And if you are growing at 40%, it will takes us far. I don't think equity is a big, big concern for me at this point. It's not like this was just kind of a tease around and then six months later, I'll need to go back to the market again. So given that there are no more surprises like COVID or anything like that, we should be good till at least INR 2,500 crores.

Moderator: Ladies and gentlemen, that would be our last question for today. I now hand the conference back to the management for their closing remarks. Thank you, and over to you.

Aalok Patel: Thank you, everyone, for joining. We hope that we've been able to answer all your queries. We look forward to the next interaction in the future. In case you require any further details, you can contact us directly or our Investor Relations teams. The contact information will be available on the presentation which is on the company website and on the stock exchange website. Thank you again and have a pleasant evening.

Moderator: Ladies and gentlemen, on behalf of InCred Equities, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.