"Equitas Small Finance Bank Limited
Q3 FY '24 Earnings Conference Call"
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Moderator: Ladies and gentlemen, good day, and welcome to Earnings Conference Call of Equitas Small Finance Bank Limited financial performance for Q3 FY '24. We have with us today: Mr. P.N. Vasudevan, MD, and CEO; Mr. Sridharan N., CFO; Mr. Murali Vaidyanathan, Senior President and Country Head, Branch Banking, Liabilities, Product and Wealth; Mr. Rohit Phadke, Senior President and Head, Assets; Mr. Natarajan M., President and Head, Treasury; Mr. Dheeraj Mohan, Head, Strategy, and IR.

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 would now like to hand the conference over to Mr. P.N. Vasudevan. Thank you, and over to you, sir.

P.N. Vasudevan: Thank you. Good evening to all of you and thank you for dialling in today. The Indian economy is doing well compared to the other global economies. However, inflation remains a sticky issue and still away from the target of 2% to 4%. India's GDP growth this year is expected to end robustly. While next year, even though moderation is definitely expected, it may still remain at an attractive level.

At Equitas, as you know, we lend to customers at the bottom and the base of the pyramid. And we continue to see a healthy credit demand, normalizing of asset quality cycles and ample opportunities from this segment to enable us to continue to build a sustainable and scalable bank.

Our business model of lending to the informal and formalizing segments through a wide range of products fuelled by deposits from the mass and the mass affluent households cater through a differential branch network has helped us weather and stay profitable during black swan key events, like demonetization and COVID.

As the impact of such events wane off, the bank has been able to deliver consistency in advances and deposit growth and return ratios. In the current year, we are going through an unfavourable interest rate cycle against a backdrop of the bank having nearly 85% of its loan book at fixed rate loans.

During the first quarter earnings call, I had highlighted the impact we may see on cost of funds and margin during the year. Also, we had discussed our focus on improving the CD ratio and how we see that moving over the next 2 years. On both these fronts, Equitas is moving as per what we had mentioned. Our NIM at 8.37% for Q3 reflects the increased liquidity on account of improved CD ratio and also the rising cost of funds.

During the past 12 months, we have improved our portfolio yield by 60 basis points and yield on fresh disbursement by over 100 basis points. And this has helped us mitigate some of the impact of rising interest rates. It's generally expected that interest rates may remain stable over the next 1 year with marginal drop coming towards the end of next year. If that plays out, we should see a reversal effect of this year in terms of NIM expansion, given our large, fixed rate loan book.

On CD ratio, as guided during the third quarter, we expect to bring it down to about 85% by end of March 25. I repeat March 25. With a CD ratio at about 91.5% as of December 23, we have completed most of the heavy lifting and the impact of further reduction in CD ratio on NIM over the next 5 quarters may be muted. When we include refinance, the CD ratio, even as of December 23, is about 85%.

On the business front, across product and customer segments, we are fairly well settled, reflected in steady advances growth. We expect to continue this and expect to end the year with around 25% to 28% gross advances growth. Overall, portfolio quality remains comfortable.

Our deposits also continued to grow well with a focus on retail assets. We would like to highlight that out of the incremental deposit mobilized during the third quarter, about 80% of them came from retail term deposits. The franchise is coming up well. And over the next few years, our strategy is to move to a customer segment approach from a product segment approach, which should help us deepen our offering for families, NRIs and digital-savvy customer segments.

Before handing over, it gives me pleasure to inform you that our trust, Equitas Healthcare Foundation, jointly with Sringeri Sharada Mutt Karnataka, have launched the Sringeri Sharada Equitas Hospital, a cancer care hospital with 100-bed capacity. Since the entire capex for the land, building and equipment are born out of the donations from Sringeri as well as our CSR contributions, we need to charge patients only for the operating cost.

Thus, our charges are about 40% of the charges of other private hospitals. And this hospital is really targeted at the middle- and low-income families to provide affordable, high-quality cancer care. And for those who come from very low income or poor families, we would be further discounting, even giving free for some of the low-income people.

With that, I now hand over the call to Sridharan, our CFO.

Sridharan N.: Good evening to everyone. Our net interest income for the quarter came at INR785 crores as compared to INR647 crores during the same quarter last year, registering a growth of 21% year-on-year. Other income for the quarter came in at INR185 crores as compared to INR127 crores during the same quarter last year, registering a growth of 46%, resulting in a net income growth of 25% year-on-year.

The total operating expenditures came at INR610 crores and remained stable with an increase of 2% sequentially. Cost to income has come down to 62.88%, which is comparatively better than Q2 of FY '24 at 64.3%. This improvement was attributed to treasury performance during Q3 FY '24 of INR30 crores as compared to INR18 crores during Q2 FY '24, a growth of 70% Q-on-Q.

Pre-provisioning operating profit. PPoP grew 29% year-on-year to INR360 crores and PPoP to assets remained stable at 3.53% for the quarter. PAT for the quarter came at INR202 crores as against INR170 crores during the same period last year, registering a growth of 19% Y-on-Y. RoA and RoE for Q3 FY '24 stands at 1.98% and 14.44%, respectively.

During Q3 FY '24, the bank has securitized and assigned advances worth of INR1,390 crores pertaining to advances in SBL, HF and VF. Based on the current advances, the bank is maintaining a healthy PCR of 55.97%. and it continues to follow stringent provisioning norms across all asset segments. The total provision for Q3 FY '24 was INR84 crores.

GNPA improved by 108 bps Y-on-Y to 2.38% in Q3 FY '24 as compared to 3.46% in Q3 FY '23. Including the securitization book, GNPA would stand at 2.29%. The NNPA improved by 67 bps Y-on-Y to 1.06% in Q3 FY '24 as compared to 1.73% in Q3 FY '23. The provision coverage ratio remains at 55.97%. As of December 31, 2023, a total CRAR at 20.24%, consisting of Tier 1 at 19.69% and Tier 2 at 0.55%.

With this, I would like to hand over to Mr. Rohit.

Rohit Phadke: Thank you, Sridharan, and good evening, everybody. Advances have grown by 31% year-on-year and 5% quarter-on-quarter. GNPA has been stable at 2.29%.

In SBL, advances have grown by 32% year-on-year and 7% quarter-on-quarter. In SBL, there's growth in non-TN businesses. As of December 22, the composition of disbursements of TN and non-TN were 65% and 35%, whereas as of last month at December end, TN disbursement had come down to 54% and non-TN disbursements have gone up by 46%. Ex-bucket collection efficiency continues to be at 99.5%.

The business seen steady growth in the states of AP, CG, Karnataka, and Maharashtra in the non-TN states. The new LoS has been rolled out and is now active in 182 branches across the country. Another 200 branches will go live this quarter.

In micro finance, advances have grown by 32% year-on-year and 7% quarter-on-quarter. 100% of all new customers acquired last quarter were onboarded using e-KYC. 95% of all new customers acquired last quarter signed the agreement, eliminating the need for use of physical agreement.

In the vehicle finance business, the used car book has now grown to 14% of the total VF advances and it has crossed INR1,000 crores. The focus here is on funding into customers for personal use. The used car market in the country is huge, and we aspire to grow this product. The focus in used CV and new CV portfolio continues to be primarily on small commercial vehicles, light commercial vehicles, and pickups.

The affordable housing home loan business is scaling up well in 34 branches in 5 states. The new LoS for this business has been rolled out in all the branches. Rural demand and macro indicators are quite positive. Things do augur well for the coming quarters. I am quite hopeful that the coming quarter will always be good.

Thank you. I'm handing it over to Murali.

Murali Vaidyanathan: Good evening. Thank you. Once again, I take this opportunity to thank you all.

Our overall focus on retail-centric approach with a differentiated approach of mass and mass affluent is continuing. And it is continuing to yield good results on three reasons. One is if you see our mobilization from the last quarter, for the last 3 quarters, we are able to maintain anything between 77% and 80% of the incremental amount, what we mobilize is through absolutely retail tickets, which is through individuals, which is through affluent individuals and also through the NR segment. I think that is one important thing that is happening.

So our continued focus on retail is helping us to penetrate us into investor segment as well as trader segment, so coupled with the fact that you see mutual fund AUM is showing a trajectory growth of 36%, couple of effects, our brokerage account, which we have a 3-in-1 tie-up, is showing very good traction of again a growth of 25%, 26% and, most importantly, ASBA helping us to actually retain SA balances. So expansion from saver to an investor to trader is significantly helping us.

As a channel, our focus on NR is now we are present in close to 120 countries through customers across and giving us a reference moat. And NR shifting into RTDs when new development, but that is helping us to grow the relationship across the spectrum. So what we are seeing is relationship backed by attractive pricing at this point of time. Consumer as a retail would like to transact more and want to hold more products. And increasingly, we are seeing products holding at a customer level and products holding at an individual level is increasing the traction.

VRM as well as normal RM channel books are growing. So overall, the trajectory looks positive. Yes, the pressure on CASA will continue to be there. And this is the first quarter after last 2, 3 quarters, I think, we have shown growth in SA also. And the increased focus on ASBA as well as trading account, I think we should develop that module. The differentiated solution in current account, for example, virtual account numbers and solution-centric approach, along with TD suite is helping us to grow the CAR account to the current accounts. So overall, our efforts are continuing to sustain this growth path.

I hand it over to Mr. Natarajan, who heads treasury.

Natarajan M.: Thank you, Murali. Good evening, everyone. Q3 FY '24 has been a relatively steady quarter on the market front. On a quarter-on-quarter basis, India 10-year yields remained mostly unchanged despite some volatility. Bond prices remained steady as market participants continued to believe that the worst of inflation and rate hike cycle is behind while continuing to avoid corroboration through data prints.

The U.S. Fed continues to be hawkish despite expectations of softening view, largely due to the ongoing fight to bring inflation below the targeted level of 2% while trying to avoid recession in an attempt at safe landing. It was a good quarter for Equitas globally. Dow Jones gained 12%. Nearer home, Indian equities continued to see a run-up, too, in Q3 FY '24 with gains of almost 11% for the frontline NIFTY 50 Index.

We scaled mount 20K on good buying from across investor classes like FIIs, DIIs, HNIs and retail. Multiple state election results seem to aid market sentiment ahead of national elections. Short-term volatility is not ruled out as we approach budget and national elections.

Geopolitics continues to be a point of concern and supply lines can be an issue, especially for oil if situation in Israel and Gaza worsens. It can result in higher inflation numbers. Despite India's economy continuing to stabilize, consolidate and grow, considering the global nature of trade and supply chain, we can expect some volatility going ahead. Hence, we view the market as cautiously optimistic.

Coming to Equitas treasury, performance for Q3 has been another steady quarter. Profit on sale of investments stood at INR27 crores. Our funding profile has been stable with opportunities available to raise funds both in the form of refinance or IBPC and securitization.

Thank you. With this, I hand it over to the operator.

Moderator: Thank you very much. The first question is from the line of Shreepal Doshi from Equirus. Please go ahead.

Shreepal Doshi: Sir, my first question was pertaining to the increase in slippages, which has also led to increase in GNPA. So could you please explain the reason behind this one?

Rohit Phadke: Our slippages have increased slightly for the reason that there have been heavy floods in Tamil Nadu. And primarily, slippages have gone up in vehicle finance and micro finance. But if you look our slippages, they have always been range-bound between 3% to 4%. I think this is we feel that this is normal and 3% to 4% is a range-bound for our business.

Shreepal Doshi: Okay. [Potential strategy as you are looking because] of the floods. So how are we seeing the situation now recovering?

Rohit Phadke: Usually, fourth quarter collection efficiencies are good. But we see that, particularly in the case of vehicle finance in the market, delinquencies have normalized. And coupled with that, the fourth quarter, generally collection efficiencies are higher. So we feel that the collection efficiencies will be much better in the fourth quarter. But we think that we have reached a normalization in the credit cycle. Because for the first 2 quarters, the credit cycle was very benign and now we feel that the market is coming back, the credit cycles are being normalized.

Shreepal Doshi: So the increase in credit cost during the quarter was also pertaining to this event only. Is that a fair understanding?

Rohit Phadke: Yes, yes, you're right.

Shreepal Doshi: Got it. Sir, second question was again on the vehicle finance side itself. So last quarter, we had rolled out the new LoS for this particular segment. And I was just listening to your earlier commentary, where we are aspirations about growing this segment. But if you look at it, the GNPAs have gone up, the disbursements during the quarter was soft. So what is it that we have in pipeline in terms of ramping of this segment incrementally?

Rohit Phadke: So the new LoS for vehicle finance has been rolled out in all the branches, and it's very active. As far as growth is concerned, advances have grown at 30%, so which is quite good. And we will continue this pace of growth in vehicle finance, right? In vehicle finance, we are only the disbursements are slightly lower because we last -- the same period last year, we had funded some low-yield strategic customers.

And low-yield products is what we have not done in vehicle finance. That is why probably you see some of the disbursements lower. But otherwise, we see a healthy growth in the market also in terms of Vehicle Finance. And we also feel that vehicle finance, particularly in new CV and used car will grow.

Shreepal Doshi: Got it. Sir, last question, just a bit on credit cost front, so because of floods and also while you said that recoveries will be held in 4Q, will there be any spillover effect on credit cost fund in 4Q?

Rohit Phadke: So see, if you -- last year, we had guided on a credit cost of 1.5%. And we landed at about 1.56%. This year, we feel that our credit costs will be at around 1.25%.

Shreepal Doshi: Okay. So we will not reach irrespective of this event at all?

Rohit Phadke: Yes, yes. And we believe that we'll be there.

Shreepal Doshi: Sorry?

Rohit Phadke: We believe that we will be at 1.25%, but we will not exceed 1.25%.

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

Renish Hareshbhai: Sir, two questions, again getting back to the credit cost one. So our nine-month credit cost run rate is 90 basis point-odd. And when we are saying our full year guidance is 1.25%, does it mean that Q4 will be higher in terms of credit cost? Or will you be significantly below the guidance range?

Vasudevan P N: So remember, in the beginning of the year, we had guided for a credit cost of 1.25% for '24 this year. So we are kind of sitting with that guidance that we gave in the beginning of the year. And we believe that the credit cost should be around that level or less than that. It will not be more than that. The question, what you're asking, is whether it will actually be 1.25% or will it be lower than that. We believe it will be lower. But we are still sticking with the guidance that we gave at the beginning of the year.

Renish Hareshbhai: Got it. And sir, just from a medium-term perspective, as you already highlighted that our normal slippage run rate will be anywhere between 3% to 4%, and even if we take 30%, 40% LGDs, so let's say, going ahead in the medium term, the credit cost range should be 1.2% to 1.5% or how you internally build the credit cost?

Vasudevan P N: See, historically, our credit cost has always remained -- I mean, if you remove some of the Black Swan years, otherwise, historically, our credit cost has always remained in the 1.1% to 1.2%.

That's where it has always traditionally been. And we believe that given our product mix and the customer segment that we lend to, on an ongoing basis, our credit cost should be typically within that range of around 1.2% and 1.25%.

Renish Hareshbhai: Got it, got it. And sir, just last question from my side. So if you look at the disbursement yield, which has gone up by almost 47 basis points sequentially, so if you can throw some light on which product is sort of driving this higher rate. I mean, across the product, we have increased it or there are a couple of products wherein we have increased the rate? And secondly, when we look at the disbursement run rate for this quarter, it's flattish.So is there some correlation between, let's say, higher interest rate and the lower disbursement? Or how do you want to get these two data points?

Rohit Phadke: So one is you asked on which products will grow?

Renish Hareshbhai: So which products you have high rates?

P.N. Vasudevan: High rates?

Rohit Phadke: Which product has increased the yield...

Rohit Phadke: So SBL, vehicle finance, micro finance, so all these three products have increased rates. Rates have also gone up marginally in the affordable home loans business. But that is marginal. Because there, you don't get very high rates. But rates have significantly gone in small business loans, vehicle finance and micro finance. This is your first question.

The second question is whether we have slowed down disbursement because of some low-yield products. Yes, see, we don't want to sacrifice NIM for the sake of only top line growth. So some of the low-yield products, we have stopped focusing. And we have focused on our high-end products. That is a yes. So the last year, we had the opportunity to do a lot of NBFC funding. And we did get our rates.

This year, there is a lot of demand for NBFC funding. But the rates, they are able to get very low rates in the market. And we don't feel that that's a great opportunity in sacrificing rates for the sake of doing top line growth. So we have defocused on those products.

Renish Hareshbhai: Got it, got it, got it. And sir, just last thing, so on the deposit side, how the market is and what we understand from outside is that competitive intensity has gone up significantly within past six, eight months. So in such scenario, how confident we are to sort of sustain this current deposit growth rate? And let's say, if not -- if that doesn't happen, how will you protect your CD ratio? I mean, naturally we have to tap along ? So how one should look at the deposit growth run rate in conjunction with the CD ratio expectation?

Murali Vaidyanathan: See, deposits, if you see the mobilization part at the retail level, between CASA and RTD, while the mix has changed, more skewed towards RTD, our ability to raise retail deposits has been in line and steadily growing up month-on-month, quarter-on-quarter, the relationship team, which works there. So our key strengths are the product we have, program we have, relationship we have, and most importantly, the price points at which we attract the customers.

So in terms of product-ship, program-ship, and engagement-ship, I think we are there. So we are fairly confident. And second thing is since it's retail and spread across mass and mass affluent and NR all contributing, we are fairly confident that in terms of retail growth, we will sustain there. Bulk is based on the requirement, okay?

The bulk is based on absolute requirement. Despite the requirement being there, as Mr. Vasu also said in the initial discussion, to be very precise, last quarter, 77% of the deposit mobilization came from only retail. A quarter before that, if you go back, it will be anything between 76% and 77%. So we'll continue to focus on retail, which continues to go granularly. And that will help the CD ratio also as chartered out until March, we're able to achieve it.

Moderator: Next question is from the line of Arvind R from Sundaram Capital.

Arvind R: I just like to understand if you can give any colour on what kind of book has been securitized? And that is my first question. And second question...

Sridharan N: Yes, the first question is clear, what kind of books have been securitized.

Arvind R: Yes, what kind of books it has been securitized, I mean, if you can give some colour on that. And second question is on -- like how would it impact the interest income? For example, if it is securitized, do we recognize it as direct assignment gain? Or like a differential is booked as interest income, like if it is booked as interest income, like where could we usually report it in the financial statement?

Sridharan N: Yes. The first question is that whatever we have done, the securitization attainment, is SBL and HF and VF loans actually. And the second question is how they are the vehicle finance is INR897 crores; housing finance, INR271 crores; and small business loans, INR222 crores, all put together, INR1,390 crores.

And your second question is how the recognition of income with regard to this one actually. See, whenever, we securitize a portfolio, our portion of the income which we receive, over and above what is paid to an investor is shown as other income as a securitization income, not as an interest income.

Arvind R: So it will be part of the other income. I mean, like basically part of the fee and other income you're saying.

Sridharan N: Yes, yes. There is no upfront.

Arvind R: Sorry, sir, there is no?

Sridharan N: There is no upfront income is recognized there.

Arvind R: Okay, okay. Only the difference is booked as part of the income.

Sridharan N: Exactly. Because this is based on the cash flow waterfall mechanism. As per that, it is recognized to a period of time based on the cash flow.

Moderator: The next question is from the line of Harish Swaminathan, an individual investor.

Harish Swaminathan: I have just one question on the employee stock option scheme, if I may. Have we done any sort of analysis as to the cost versus benefit of the scheme with respect to you know this benefit is, of course, if we can retain employees. But the cost is that it dilutes the equity. And so instead of that, if you pay out the market salaries, then if they're interested, they can buy the shares.

So and is there any sort of threshold which we don't want to breach with respect to comparable banks? Because it dilutes the equity on the one hand. But yes, we hope to the employee has a vesting period of, let's say, four years. But instead of that, if you pay him market salaries, then he decides whether he wants to buy or not. So I just wanted your thoughts on that.

P.N. Vasudevan: Yes. So we had an ESOP scheme, which was formulated a very long time back. And when we did that really 2007 or 2008, when we formulated the ESOP scheme when we were an NBFC, so we had set aside certain options under the pool, ESOP pool. And that was about 15% of the capital at that point in time.

So subsequently, I think once we added to that pool maybe about six or seven years back. Today, there are a number of options available in the pool to be granted, will work out to maybe about approximately I mean, off memory, I'm not very sure, but off memory, it should work out to maybe about 4% of the or maybe 3%, 3.5%, 4% of the equity of the bank.

In terms of dilution, of course, as we all know, ESOPs can do dilute their shareholders. But then it benefits the employee to whom it is offered. And it's part of the compensation package and compensation structuring. And so it's something that we expect should help improve retention in the system of people who are good performers.

ESOPs, there are many ways of offering it to the employees. In Equitas, what we are adopting currently is that ESOPs are offered to employees at the end of each year of business performance. Based on their performance and based on their appraisal rating, ESOPs are granted based on their position or level in the system. And once the ESOPs are granted, they vest after a period of 12 months.

And once they vest, they can be exercised within three years from thereon and all options are granted. At the time of grant, they're already granted at their price of the previous closing price of the previous day. Then further, ESOPs are -- the grant price is taken as of the closing price of the previous day to the date of grant. That's how it is done. We do believe that this is something which is a very highly motivating instrument from an employee retention perspective.

And I'm sure you would have seen in other organizations, and in Equitas, we have definitely seen many instances where people have seriously and significantly benefited from the value of value accrued under various ESOP schemes. And that's something that overall helps build a further level of loyalty or commitment to the system.

Moderator: The next question is from the line of Abhishek Murarka from HSBC.

Abhishek Murarka: So my first question is on disbursement yields. I think, can you share the disbursement yields for SBL, VF and MFI for the quarter?

Rohit Phadke: Abhishek, just a minute. Overall, our yield has gone up from -- three products, SBL, VF and MFI. MF is constant at 25%. We've increased it from 24% to 25%. In vehicle finance, I don't have the overall -- one second, one second. Okay, I'll give you the top segment. The used CV, we have grown from 18.28% in March to 19.56% in December. In new CV, we've grown from 12.32% in March to 13.69% in December. In SBL, we have grown from 16.33% in March to 17.16% in December.

Abhishek Murarka: That's very useful. And these are the disbursement yields?

Rohit Phadke: Yes, yes, these are the disbursement yields, these are not the portfolio yields.

Abhishek Murarka: Understood. And passing on these yields are is easy or, I mean, you're finding it incrementally difficult to take further yield hikes? So in your customer segment, how is the competition playing out, if you can talk a little bit about that?

Rohit Phadke: Yes. As we keep saying that we lend to the under-banked or the bottom of the pyramid. So we don't find much difficulty in increasing the rate. But we also have to keep in mind that there has to be a threshold that there has to be also there. Affordability has to be borne in mind. That is one thing that we have to keep in mind while increasing the rate.

Abhishek Murarka: Sure. So the disbursement, if I were to tie it back, basically the slowdown in disbursements this quarter on a sequential basis, that was more to do with just trying to align with the CD ratio goals. And now incrementally, should we see a sort of pick up again in the following quarters?

P.N. Vasudevan: No, no, no. The disbursement and CD ratios are really not committed because we have been able to mobilize extra deposits to ensure that we meet our CD ratio requirement on an ongoing basis So, that's really not a reason in terms of disbursement at all. So I think the disbursement is moving quarter-to-quarter. If you see the Q2 was higher and Q3 was lower in disbursement. That is the only because of certain specific reasons such as maybe a lot of holidays, maybe a lot of rain disruptions in different parts of the country in the third quarter, etcetera. But these are very normal and I think they are so long as they are within a certain range, I think they are generally comfortable.

Abhishek Murarka: Right. But incrementally, Vasu, the disruptions are over and now it is business as usual and that we should resume growing in each of these segments. Is that a fair way to look at?

P.N. Vasudevan: I mean, even with all those disruptions, we have done a 32% advance growth on a gross basis for the nine months. It is very comfortable. I don't think that's something that we need to be, we are at least concerned or worried about. And so these kinds of disturbances will be there. Holidays and rains are some things that's part of life. So they will keep coming at various points in time. So if you see Q2, there are certain parts of the country which faces rain. In Q3, some other parts of the country face rain. So these are things which will happen.

And to that extent, there will be some level of range within these disbursements will move or get in faster. But on an ongoing basis, these are normal things and business doesn't really get affected too much because of that. So you may have a small dip here or a small increase in some other area. But these are within normal ranges and so they don't really account for a factor which should raise that as a concern.

As we have mentioned earlier, we have been guiding that we should, on a sustainable basis, look for about 25%-plus level of growth on an ongoing basis and that's something we believe should be possible over the medium term.

Abhishek Murarka: Got it, got it. And just the second question is on costs. So we've seen now a bit of improvement in costs for a few quarters. Should this secular trend continue? Or again, we could see some or is there any impending spend, let's say, on technology or big branch expansion plans or something in the pipeline?

P.N. Vasudevan: So on cost of operations, we have been saying, and I think that's something that we have been saying fairly for a long time, that we are still a fairly evolving bank. So we are going to be seeing cost of funds at very similar levels to where we are. Yes, there has been a drop in the last two quarters. But again, you may remember that in the first quarter, our cost of operation always jumps higher because there's an increase given to the staff, the yearly increment given in the month of April and that always takes the first quarter cost to a higher level. And subsequently, that gets leveraged over the year. And that's what is flowing out in the second and third quarter. So if you look at the further investment required in the bank going forward, technology is one area where some amount of investments will keep going in. Second thing is, we have mentioned it earlier, there are two big products coming along the way. One is our AD-I project and the other one is credit card launch. The AD-I project is underway and there's going to be some amount of investments we need to make both on tech and on people to get us enabled and ready to commence that business. And credit cards, again there's going to be an investment both on tech and on people before the product will go live.So these are the two products where some investments will come shortly in the future. But otherwise, if you see branch expansion, as we have mentioned in the past also, we have put up a very large number of branches quite early on. And so thankfully, the cost of increasing our network of branches is behind us. So that is not something you should see -- for the next at least 2 to 3 years, you won't see too much of increase in cost because of branch expansion. That's one thing.

Second thing is that other than these two new products, so credit card and AD-I, we don't really see any particular new /other new products coming into the system. So there is most of the products that we have already invested and many of the products will become profitable across their loss-making cycles and become profitable. The affordable housing is still at an early stage. But this year, they should break even and the next 2 years, they should be pulling their full weight in the system. So minus credit card and the AD-I, we are all really not looking at any other major product investment.

So product investment, offset of these two and branch network investments, are something that we have done in the past, and we are getting the benefit of that today. Going forward, tech investments in these two products are the ones where we should be noticing the success of our branding. So to some extent, you can say our cost will be at this level, give or take, 1% or 2% on a quarterly basis moving up and down. But otherwise by and large, I think we should remain at this level.

Moderator: The next question is from the line of Sarvesh Gupta from Maximal Capital.

Sarvesh Gupta: Sir, just a follow-up on the previous question, so I mean, we are having a very strong growth in our overall top line. So given that, I mean, why would you expect, let's say, in the medium term, 2 to 3 years, for the cost to income to remain at the same level? Is it just because of the newer products which will have losses which will be large enough to be to keep the cost at a elevated level?

P. N. Vasudevan: Yes, absolutely, absolutely. I think there is going to be a fairly large amount of money, which has to be put behind those two products and the related technology platform that needs to be created. We don't have any of that. We don't have the treasury system for managing forex. We don't have the foreign transaction settlement systems. And we don't have the effort and tools for monitoring fraud risk management of foreign transactions. We don't have any of that today. So the technology behind all of that needs to be put in place on the credit card. Again, the entire thing has to be put in place .I mean, the elements for the loan management system for credit card is first and then that has to be integrated with other systems. So there is a large amount of investment required on both. And probably we'll spend most of our money before we even start the product. And then the product is going to take time to get going and then turn breakeven and then become profitable.

So there's maybe a 3-year kind of a time frame by which we will probably fully pull their weight on the system. And that is the time when the investments will have to be supporting these products.

Sarvesh Gupta: And is it possible like the two projects you mentioned, AD-I and CC, is it possible to quantify or give a range of the investments that we are contemplating in these two areas?

P. N. Vasudevan: Yes, we will do that. So to my point, I think we'll note that down. Next quarter, when we come back, we will give you the data. Yes, we will give you a good amount of idea of the kind of money that we are going to invest in these two and also give you some maybe a ballpark idea in terms of the launch date and also the likely break-even time span. So we'll give all of that in the next call.

Sarvesh Gupta: And just finally, next year, you would expect broadly NIM to be in the same range or increase a little bit in case the interest rates go down? Or do you expect any pressure because of a mix change, any further pressure on the NIM?

P. N. Vasudevan: Actually, if you see our model, we had an 85% fixed rate loan book model. And so we have had the worst of the time during the current financial year, right? We have really gone through the worst of the time when the interest rates have really sharply gone up. And our yield on advances remain sticky because they are all fixed rate loans. We are not going to be able to refi for our existing borrowers.

And we did increase our lending rate. We have mentioned that our disbursement yield went up by 1% over the last 1 year whereas our portfolio yield has gone up by about 0.6% over the same period of 1 year. And the NIM has contracted by nearly about 75 basis points or 0.75% over the same period.

So because of that, the NIM has contracted. But in spite of all of that and in spite of continuing to invest in technology and in the new products, we are able to deliver an ROA and ROE which is at fairly reasonable levels of around 2% and 15%, respectively.

So that shows basically the underlying fundamental profitable model of the bank. Now going forward, that's going to be interesting. The next year is going to be really interesting because there are three scenarios. Interest rates can go further up. Interest rates may flatten out and remain at this level. And interest rates in the next maybe 3 quarters or 4 quarters may start coming down. Now if the interest rates go up, we are going to see a repeat of what we have seen in the current year, our NIM should go down.

But however, if that does not happen, if interest rate remains even flat, forget going down. Even if it remains flat, we should see our NIM starting to improve because our advances yield has been growing as we have mentioned, right, and our interest cost will start flattening out. The rise in the interest cost will stop. We have taken most of the hits, I believe.

In the fourth quarter, there will be further increase in the interest cost to some extent. And in the first quarter of next financial year, there will be again a marginal increase in the interest cost because we still have some old deposits coming up for maturity.

But from the second quarter of next year onwards, the interest cost may not really go up at all, assuming the rates remain flat. But our portfolio yield will continue to rise because of the current year disbursement being at higher rates, as a percentage, contributing more to the portfolio as the old book runs down. So we should see an improvement probably in the next financial year, even if the interest rate remains flat. And that is where things are going to be really interesting for Equitas.

Moderator: The next question is from Ashlesh Sonje from Kotak Securities.

Ashlesh Sonje Sir, just a couple of questions, firstly, on the slippages front, specifically in the MFI book, the GNPA ratio has gone up by 50, 55 basis points Q-o-Q. So any specific geography, which has seen a higher deterioration in asset quality that you're going to call out?

Rohit Phadke: Yes. So we have said the floods have affected the southern districts of Tamil Nadu, which is Tirunelveli, Tenkasi, Tuticorin. Basically, for us, it's a division called Madurai division. So that is where we have seen slightly higher slippages.

Ashlesh Sonje: Okay, perfect. And secondly, on the yield front, would you take a look at the product mix within SBL, the subsegmental mix across micro-LAP, business loans and general LAP to pop up yields? Because that mix has been fairly steady over the past few quarters.

P. N. Vasudevan: Yes, we do look at the yield, Ashlesh, because when we increase the yield on advances, it is done on a per product. It is not being done overall for the business. So you see, so what happens is, so when you have to add in a certain yield, so you do it based on the potential of that product and the potential to increase the yield. In SBL, we don't see any reason why any product should decrease in terms of disbursements because there is ample market for each of those products. So we have not decreased anything. We have increased yield for every subsegment of SBL.

Moderator: The next question is from the line of Pallavi Deshpande from Sameeksha Capital.

Pallavi Deshpande: So just carrying on, on the previous question, the SBL increase in yield...

P. N. Vasudevan: Is it not audible?

Pallavi Deshpande; Yes. On the SBL portfolio, what would be the slippage for that portfolio quarter-on-quarter?

Dheeraj Mohan: Yes, we haven't given product-level slippages. Yes, so we'll leave it at like that. We don't disclose it.

Pallavi Deshpande: No, I was just trying to wonder if they're not just...

Dheeraj Mohan : Yes, we've given you an indication that it is micro finance and micro finance-like.

Pallavi Deshpande: Yes, yes. And so just -- okay, just to put it another way, is there any -- like you said, the increase in rates, how does that effect the asset quality for SBL? Is there any deterioration there because of that? And how do you see it long term? How much capacity do we have to increase each year, so it will go up like you said?

Rohit Phadke: So there is no decrease in the quality of SBL. SBL GNPAs are as good as they were the last quarter. Ex-bucket collection efficiency, SBL is stable at 99.5%. So the increase in yield for SBL has not led to a deterioration in any quality in terms of SBL.

Moderator: The next question is from the line of Shailesh from Centrum Broking.

Shailesh: Sir, I just wanted to understand, for the 9 months, we have done excellently well on the deposit side in spite of the heightened competition in that, right? So that has brought down our CDR. So going ahead, would we continue this same pace? Because I see our deposit growth has outstripped the advances growth. So how do we see that or we would take a pause in a quarter or 2 for protection of NIM?

P. N. Vasudevan: Yes. So as I had mentioned in my opening remarks, we had looked at reaching a CD ratio of around 90% by March '24. So we are at about 91.5% by December. So we'll aim to move to 90% by March '24 and we are also looking to take it down to around 85% by March '25, which is the next financial year-end.

So as I had mentioned in my opening remarks, most of the heavy lifting on CD ratio has been completed and is behind us now. So from here onwards on a quarterly basis, we will be moving the CD ratio on a smaller measure to reach whatever that we are looking at as our outcome and which really means that the need to mobilize extra deposits over the next few quarters would come down compared to what we did in the second and third quarter.

Shailesh: Okay, fair enough. So apart from asset book repricing, which is one more lever which will help our NIM in the next few quarters. Is that understanding right?

P. N. Vasudevan: Sorry, sorry, your voice is not clear.

Shailesh: Yes. So I was saying that apart from asset book repricing, this would be one more lever at our disposal for a NIM expansion next year?

P. N. Vasudevan: Yes, yes, that's right. So going forward, we believe that the NIM impact from interest rate scenario will still last maybe to some extent in the fourth quarter and marginally in the first quarter. Hopefully, after that, it should flatten out or start even improving. The NIM impact, because of CD ratio coming down, that will still be there. But it will be very marginal going forward.

And if you remember in the beginning of the year, we had also guided on the NIM, that the NIM was 9% for last financial year. And in the beginning of the year, we had mentioned that for this current financial year, we should be looking at around 8.5% NIM for the full year as a whole and also a possible 8.25% exit NIM for the fourth quarter. It's what we had mentioned in the beginning of the year. And I think more or less, the numbers are in that level.

Shailesh: Sir, that's helpful. Sir, one more question. One is that some of our peers in enterprise segment have decreased lending rates, and we have increased, right? In the past 3 quarters, we have increased not only MFI, other segment as well. So how do you see the competition scenario? And does that affect the growth outlook for FY '25? I know you have guided that we maintain the growth of upwards of 25%, but just wanted to know your view in terms of where peers have been reducing, especially in the MFI segment.

P. N. Vasudevan: Yes. So we don't see any impact on that.

Moderator: The last question is from the line of Sameer Bhise from JM Financial.

Sameer Bhise: Congrats on a good quarter. What you highlighted that there could be three scenarios on interest rates, and especially thinking about the scenario of rates coming off probably 3 to 4 quarters down the line, how do you think from the point of view of probably a higher margin opportunity?

Would you like to let that benefit flow to the ROA level or you have -- you would continue to invest with respect to some of the newer initiatives? How should we think about this? Because already, we are seeing some amount of improvement on cost to income. Credit costs have normalized. Margins have come off and still we are clocking a 2% ROA. So some outlook there would be helpful.

P. N. Vasudevan: Yes, good question here, very nice question. And if you remember, I'm sure many of you may not remember, but long back, I'm really talking of long back, maybe, let's say, 2 or 3 years back, we have always been mentioning that ideally a bank like ours, given the kind of consumer segment that we lend to, a bank like ours should be looking at an ROA of around 2.25%-plus. That's what we have been saying.

Because there is an inherent level of risk in the portfolio that we'll have because we are lending to a segment of customers who, while their repayment records have been excellent with us, however, they are fragile to any market events like the black swan events that we have seen in the past. So to offset that risk, the return also has to be compensatory. And so a 2.25%-plus kind of an ROA is what we have been always saying, should be -- what we should be looking at from a model like ours.

And so this question of next year or subsequently, if the rates either remain constant or maybe come off a bit over time, the impact that it should leave on the positive impact of that on the on the NIMs or on the PPOP, should ideally flow down to the ROA level. And hopefully, we should try and reach that 2.25%-plus during that kind of event.

Moderator: Thank you. Ladies and gentlemen, that was the last question for today. I would now like to hand the conference over to Mr. P.N. Vasudevan for closing comments.

P. N. Vasudevan: Yes. Thank you, and thanks for all of you for dialling in. I know we have another call now, let's all hurry into that. See you. Bye-bye.

Moderator: Thank you. On behalf of Equitas Small Finance Bank Limited, we conclude this conference. Thank you for joining us. You may now disconnect your lines.