"Equitas Small Finance Bank Limited

Financial Performance Q2 FY '24

Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day, and welcome to the Earnings Call of Equitas Small Finance Bank Limited's financial performance for Q2 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 morning, and thank you all for dialing in this morning. On the macro front, India's GDP growth continues to be quite resilient and all lead indicators like e-way bills, 3-wheeler sales, 2-wheeler sales, manufacturing, construction activity, so we see a good amount of activity across the sectors. And all this seems to indicate a favorable environment. And with the festivals coming in, in the second half of the year, we expect cash flows to improve in the hands of people, which we hope will help us end the year on a strong note.

On the ground, we continue to see good demand across product segments that we operate in. And segments like commercial vehicle finance, small business loans, all the lead indicators in these segments are quite healthy. This gives us a comfort to grow the higher-yielding products within these segments.

Our advances have grown by 37% year-on-year. However, we must remember that last year, the first half was muted, while we had a very strong robust growth in the second half. Hence adjusting for the base asset, we believe that the advance of growth for the full year should be in the range of around 25% to 30%.

Our portfolio quality continues to give us a lot of comfort. We are a 15-year-old NBFC turned bank. During this 15 years, except for two external event-led stress in the form of demonetization and COVID, we have never seen a stress in our portfolio. Given our focus on sourcing channels, which is largely in-house and strong credit process, we believe that our portfolio quality should remain good, giving us a comfort to pursue sustainable growth.

On the deposit front, we continue to see strong traction in Retail TD, leading to an overall healthy growth of around 40% in deposits year-on-year. CASA is an area of focus for the bank, and Murali will deal with initiatives that are being put in place to grow the CASA book going forward. We have seen an increase in interest cost and decrease in NIM during the quarter based on the level of old deposits maturing and getting replaced with new deposits in the second half.

And I've guided in the first quarter, we expect interest costs to go up moderately over the rest of the year to about 7.5%. With the benefit of increase in lending rates effected over the last few months coming in, we expect the NIM drop to also moderate and remain within the earlier guidance.

Finally, I'm happy to share that as part of our CSR initiative, jointly between Equitas Healthcare Foundation and Sringeri Sharada Mutt, the Sringeri Sharada Equitas Hospital has become functional. These are principally cancer care hospital with other multispecialty also offered. The aim here is to provide high-quality health care at very affordable rates to people from low-income segments.

Thank you. And with this, I hand it over to Rohit.

Rohit Phadke: Thank you, Vasu sir. Good morning, everybody. Advances have grown by 37% year-on-year and 6% quarter-on-quarter and have crossed INR30,000 crores. There's a reduction in the GNPA to 2.1% from 2.6% in the previous quarter. Collection efficiencies across businesses are stable.

In SBL, advances have grown by 32% year-on-year to INR11,550 crores. In SBL, our trust on growing the non-TN business continues. Non-TN disbursements were at 42% for the quarter as against 39% for the first quarter. The business has seen growth in the states of Andhra Pradesh, Telangana, Karnataka and Maharashtra. The new LOS is now active in 300 branches across the country and will be fully operational across all the SBL branches by the end of the year.

Microfinance, the industry has grown by 19.5%. But microfinance NBFCs have seen a higher growth of 38%. We have grown by 41%. Ex-bucket collection efficiency is stable at 99.4%. The CV industry has seen a growth of over 3% quarter-on-quarter, and demand remains strong. Our focus continues to be on LCV and small commercial vehicle in the used CV segment and on small commercial vehicles in the new CV segment.

In used car, our focus is on the personal use segment. Used car advances have now just near INR1,000 crores. The affordable home loans business continues to scale up well. The coming quarter is a festive quarter, and I expect the demand to remain strong. All indicators seem to be positive, and I do hope that we have another good quarter.

Thank you so much. I'm handing over this to Mr. Sridharan -- Murali, sorry. I'm handing this over to Murali.

Murali Vaidyanathan: Good morning. As we are inching up towards the festive season, our quarter 2 results would actually cheer up all and for us, too. And in terms of deposit mobilization, we continue to have the retail focus, and we are happy to say that the newly launched 444 days, a 1-year plus product which was actually the need for the hour across the segments, including HNI, senior citizens, has taken off very well.

In fact, last quarter, our mobilization, 70% to 75%, came through 444 days as a focus. So our retail focus in terms of acquiring customers is taking propulsion, and to take -- facilitate that, 444 days, our newly introduced product, has actually helped us.

Second important initiative is our institutional business last quarter shown us a good traction in terms of overall deal as well as CASA in terms of customer acquisition. So just to give you an insight, we, in the first half, has done close to 1,10,000 FDs to be very precise and among 80,000 unique customers. So this shows the intensity of new customers coming in as well as old customer preferring TD as a preferred route.

NR business has crossed INR1, 000 crores of TD, we are now present in 100 countries, and that is one incremental but significant learning and milestone for us.

Last but not the least, our digital solutions at this point of time is fully propelled with VKYC-backed. Our VKYC and full KYC conversions are all-time high. So overall, we will continue to have the focus of retail. We will continue to hold INR1 lakh to INR1 crore bucket, and Elite proposition getting strengthened and strengthened.

With this note, I would like to hand it over to Nat -- Sridharan.

Natarajan M: Natarajan here from Treasury, yes. Good morning, everyone. The quarter went by has been a slightly challenging quarter in the market front. Bond prices went as yields hardened on the back of surging U.S. 10-year yields, even the U.S. Fed continues to issue hawkish statements on their ongoing fight to bring inflation below the targeted level of 2%. Indian equities continue to see a run up in Q2 FY '24, with modest gains of 2% for the frontline NIFTY 50, where the broader mid-cap and small cap indices have gained more than 13% and 17%, respectively.

Foreign investors, however, turned net sellers in both equity and bond markets. RBI continues to maintain status quo on interest rates, with emphasis on bringing inflation down to 4%. Possibility of OMO sales to drain excess liquidity has changed the interest rate outlook in the short term. Global cues also point to nervousness as U.S. yields continue to spike, and higher-for-longer rates indicate U.S. could enter a brief period of recession.

Worsening geopolitics, especially in Middle East region, could result in spike on crude prices, effectively challenging -- effectively channeling into higher inflation numbers. Despite India's economy continues to stabilize, consolidate and grow, short-term volatility is not ruled out as we approach multiple state elections ahead of the national elections next year. Hence, we view the market as cautiously optimistic.

Coming to Equitas treasury performance for last quarter, it's been under a steady performance. Profit on sale of investments stood at INR23 crores. Our funding profile has been quite stable, with opportunities available to raise funds both in the form of refinance as well as IBPC.

With this, I hand it over to Sridharan.

Sridharan N: Thanks, Nat. Good morning to everyone. Our net interest income for the quarter came at INR766 crores as compared to INR610 crores during the same quarter last year, registering a growth of 26% Y-o-Y. Other income for the quarter came in at INR161 crores as compared to INR115 crores during the same quarter last year, registering a growth of 40%, resulting in a net income growth of 28% year-on-year.

The total operating expenditure came at INR597 crores as compared to INR483 crores during the same quarter previous year. The operating cost has increased by 3% Q-on-Q and 24% at Y-o-Y basis.

The bank continues to invest in loan origination system, customer apps and other enhancement features for better customer experience. Despite this spending, the cost to income is maintained at 64.3% level, which is comparatively better than Q1 FY '24 at 65.05%.

Pre-provisioning operating profit, PPoP, grew at 36% year-on-year to INR330 crores, and PPoP to assets remained stable at 3.38% for the quarter. PAT for the quarter came at INR198 crores as against INR116 crores during the same period last year, registering a growth of 70% Y-o-Y. ROA and ROE for Q2 FY '24 stands at 2.03% and 14.62%, respectively.

During Q2 FY '24, the bank has sold NPA assets for INR162 crores to ARC, which resulted in an excess provision reversal of INR23.04 crores in the P&L. We have made additional provision of INR28.03 crores, and the total provision for the quarter is at INR63 crores. GNPA improved by 48 bps at 2.12% in Q2 FY '24 as compared to Q1 FY '24 and improved by 170 bps as compared to Q2 FY '23.

NNPA improved by 21 bps at 0.91% in Q2 FY '24 as compared to 1.12% in Q1 FY '24 and 1.93% in Q2 FY '23. The provision coverage ratio remains at 57.72%. As of September 30, 2023, the total CRAR at 21.33%, comprising of Tier 1 at 20.65% and Tier 2 at 0.68%. PAT of INR390 crores for the half year was not considered while computing CRAR as per the RBI guideline.

With this, I would like to hand over to operator, and we will be happy to take questions from your end.

Moderator: Thank you very much. We will now begin the question-and-answer session. Our first question is from the line of Darpin Shah from Haitong India.

Darpin Shah: So my first question is, if you can just explain this ARC sale once again, please?

Sridharan N: About the ARC sale, which we made in this quarter, we have made a sale of INR162 crores worth of NPA advances. And we had -- as I told you, we have taken to INR23.03 crores to the P&L. The entire consideration was received was INR118.19 crores, consisting of cash consideration of INR57.91 crores and security of INR60.28 crores and we have made a provision of INR47 crores on the security receipts.

Darpin Shah: And my second question is on what will be the drivers for ROA now because when we see margins are coming down, our loan loss provisions will largely are at bottom at 80 basis points, and cost-to-income or cost-to-assets is still at around 6% plus. So, what will be the drivers for our ROA, if you can just guide us on that?

P.N. Vasudevan: So, if you see the model, our -- the interest we are now more or less nearing the bottom of the interest rate cycle scenario. Our interest cost has already moved to 7.21% in the second quarter.

And based on the quantum of deposits which are coming up for repricing the old deposits which are coming up for repricing over the second half over the next 6 months, we expect that the interest cost would move up moderately from here on for the rest of the 6 months of the year.

So, we expect the interest cost to move to around 7.5% over the next 6 months, which is more moderate than what really happened in the second quarter because most of the deposits mature in the second quarter.

Second thing is that we have increased the lending rates in different products on the loan side over the last few months and the benefit of that we expect to kick in over the next few months and quarters.

So, third thing is that seasonally, the second half of the year is generally more robust from a disbursement perspective. So, that should again see some improvement from a fee income perspective.

So, a combination of all of this is what we expect that the effect on NIM should be a little bit more moderate over the second half of the year compared to the first half of the year. And so that's where we expect the spreads, the PPOP to kind of hold and the credit cycle we expect to continue to be quite benign for the rest of the year also.

At least as of now from a market feedback perspective, our portfolio continues to do quite well and we don't particularly see any indicators which could reverse that. So, given all of this, I think in spite of the fact that we have had the worst year from an interest rate cycle perspective, I think the bank has done reasonably well from an overall management of the financials in the bottom line.

And assuming -- I mean we don't know. Nobody can predict, but assuming that the interest rates remain -- is not going down, at least, if they remain at the current levels for, let's say, the next 12 months or so, we should actually then start seeing the positive benefit of the interest rate scenario on Equitas because as in Equitas almost 85% of our loans are fixed rate loans.

So, if the interest rates even remain where they are with the increased lending rate that we affected over the last few months the benefit should actually start going to the opposite side. So, that's basically how we expect the bottom line to play out.

Darpin Shah: Just how much lending rates you would have increased over the last 6 months?

P.N. Vasudevan: So, it depends on different products. So, it's very difficult to get on product by product. But anyway, at the overall level, we will keep presenting it in our portfolio yield, that will reflect on the overall portfolio yield. But individual products, there will be differences in terms of what we do.

Moderator: Thank you. Our next question is from the line of Shreepal Doshi from Equirus Securities. Please go ahead.

Shreepal Doshi: Hi, sir. Congrats on good numbers. Sir, my question was on opex. We are in an investment phase and while we are working on upgrading our tech as well as coming out with applications, but if you look at our AUM growth is much higher versus our opex growth. So, what is the opex run rate that we are likely to see for the second half?

And we have seen opex to -- sorry, cost-to-asset ratio coming off on a sequential basis. So, are we restraining on any of our -- this tech drives in order to attain that 2% ROA in mindset?

P.N. Vasudevan: See the -- historically, what happens is that the opex goes up sharply in the first quarter because there is a -- on an average about 10% increase in staff cost. And in Equitas, if you just notice the staff cost is almost 65% of our total operating cost. And so when that goes up by 10% in the month of April, it has a very sharp effect in the first quarter.

And obviously income cannot go up at the same level in the first quarter. Income goes up, spread over the entire year and so we always have a negative jaw between income growth and opex growth in the first quarter. And then slowly, that jaw starts reversing and towards the end of the year, it's actually completely reversal.

So that's the trend that we have seen always, and that's the trend that plays out this year also. So, in the first quarter if you see the opex growth, year-on-year opex growth for the first quarter was higher than the income growth, whereas when you look at the second quarter, the picture is reversed. The income growth is higher than the opex growth, even if it's only marginal, but it is reversed.

And third and fourth quarter, we expect that to continue to expand because the opex growth will not have that kicker of staff cost increase, while the income should continue to reflect the growth in business. So that's how it is and this year also, I think that's how it will play out.

In terms of our investments, there is no kind of stopping of any of our investments. As you have mentioned, a few major IT projects have gone live already. Our entire CVs upgrade got completed in the first quarter. We have put in place a comprehensive enterprise data warehouse, EDW, that project got completed in the second quarter.

So, the LOS for vehicle finance has gone live fully now, and that has now become functional across all vehicles finance branches. The LOS for the retail, which is a small business loan and housing finance, so that is underway now. I think about 200, 300 branches have gone live with that and the remaining 150-odd branches will go live over the next maybe 2 months, 3 months.

Then in terms of other two major projects, the CRM -- the new CRM project that we are working on, that's expected to go live by the fourth quarter. The IBMB, which we have mentioned in some presentations earlier, the IBM app we are doing a bottom-up native development of IBM app with the help from IBM.

And that also is progressing very well, and we expect that to go live again in the fourth quarter of this year and that should actually give a very different level of customer experience for people who use our IBM app and also help the bank in terms of giving a different feel of the IBM app based on the profile of the customers we can profile, we can actually differentiate the app based on the profile of the person who logs in.

So, all these projects, there's no stepping back on any of that. So, the entire journey that we have been undertaking on that continues. Besides that, as we mentioned earlier, the major investments are going into the product development. So, the personal loan, we have spent some money to develop our personal loan product, and that might go live by the fourth quarter of this year.

The AD-1 license that we got the -- we got the AD-1 license from RBI recently, and a lot of work is undergoing on that and we expect that the first set of products under our AD-1 category should go live by the first quarter of next year while parallelly the project team -- there's a project team that we have put in place for our credit card launch.

And so the negotiations are on with the vendors on that, but we have scheduled to go live by second quarter of next financial year, which, as of now, looks broadly reasonably in place. So, you see that across the system, whether it's tech development or in product development, we have really not been compromising on any of our spending. And so we believe that these are things which will really help the bank sustain its growth and profitability over the medium to long run.

Shreepal Doshi: Got it, sir. Thank you so much for the detailed answer. Sir, just another question on credit cost rate...

Moderator: Sorry to interrupt Mr. Shreepal Doshi, may we request that you return to the question queue for follow-up questions as there are several participants waiting for their turn. Thank you.

Shreepal Doshi: Sure. Okay. Thank you.

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

Rajiv Mehta: Yes, sir. Hi, congrats on a very good set of numbers. So sir, firstly, on -- how much higher will be the disbursement yield versus the portfolio yield? And if you can comment about the movement in 31 DPD to 90 DPD bucket, have you seen any reduction? Or maybe if you can comment versus where we are -- what it used to be pre-COVID just to get some idea about slippage?

Rohit Phadke: Hi, Rohit here. So can you please repeat the question, sir?

Rajiv Mehta: Yes. So the first question was about, how much higher will be the disbursement yield versus the portfolio yield, which is reported at 17.4%?

Rohit Phadke: Right. So disbursement will be -- it is distributed across products. It will be difficult for me to tell you each yield because there are multiple products. There are multiple sub-segments in each segment, right? So it's very difficult. So for instance, in UCV, it has gone up by 1%. So similarly, there will be very different yields across. It will be very difficult for me to tell you the disbursement yield for each product.

Rajiv Mehta: Okay. If you can just quantify the disbursement -- blended disbursement yield for second quarter disbursement?

Rohit Phadke: Okay. Just a minute.

Dheeraj Mohan: Yes, this is Dheeraj here. Yes. I just – okay, Rohit.

Rohit Phadke: Yes, I have it. So it's close to about 18.3% is our yield on disbursement for the latest quarter.

Rajiv Mehta: Okay. And -- yes.

Rohit Phadke: So if you want to break up, see for SBL, it was 16.3% in March, and it is now 16.96% as of September. In case of CV, it was 15.96%, and it is 16.96% today. These are the disbursement yield.

Rajiv Mehta: Okay. And the second thing, I had asked was on 31 days to 90 days, the SMA 1, SMA 2 bucket. Has there been any reduction? And where is the bucket versus what it was pre-COVID?

Rohit Phadke: In 31 days to 90 days, it was [3.3] in the first quarter. And it's now marginally at about -- flat at about 3.26%.

Rajiv Mehta: Got it. Yes. Thank you so much.

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

Nidhesh: Thanks for the opportunity, sir, and congratulations on a good set of performance for Q2. First on margins, if you look at your loan spreads have remained stable. We have seen 30-basis-point improvement in yields and 30-basis-point improvement increase in cost of funds. But despite that, we have seen margin decline of 30 basis points. So what explains that? And should we further expect yields to go up given that our back book is fixed and despite that, we have seen sharp increase in yields in this quarter?

P.N. Vasudevan: Yes, you're right. We should see a further uptick on that because as Rohit just mentioned to the previous question, the disbursement yields have been going up, and the full benefit of that will only come over a period of time. So we are just beginning to see that effect, and hopefully, we should see further improvement in that as we go by. And given that, it's largely a fixed rate loan book, obviously, it will be there on the system for some time to come. Yes.

Nidhesh: And sir, on the margins, despite loan spreads being stable, our NIMs have declined by 30 basis points?

P.N. Vasudevan: Yes. So that's a combination of the fact that there has been an increase in the quantum of deposits because the deposit has grown by about 41% for the quarter compared to 37% of advances growth. So there has been an incremental growth in deposits, which has been invested in securities, in corporate bonds. So that is having that effect -- marginal effect from a NIM perspective.

Nidhesh: Thank you.

Moderator: Thank you. Mr. Nidesh, may we request you to return to the question queue for follow-up questions, please. Thank you. Our next question is from the line of Shailesh Kanani from Centrum Broking. Please go ahead.

Shailesh Kanani: Good morning everyone and thanks for the opportunity. Sir, I have two questions. One is on the gross slippage front, there has been a sequential hike. So how do we view that? And also on our CDR, though there has been a sequential improvement in CDR ratio, but it seems to be on the higher side. So can you just highlight both this thing?

Rohit Phadke: So I'll answer the question on the credit -- on the gross slippages. The slippages are marginally higher. And most of the slippages have come from the CVs. So CV cycle, if you look at it, because of the first -- because of the monsoons, generally, CV -- weak collection in the first six months, and the collection drastically improved in H2. So most of the slippages from CV, and we -- I expect that all those slippages will be covered up in the next six months.

P.N. Vasudevan: On the CD ratio, without reckoning the refinance from institutions, the CD ratio is about 94.5% for the second quarter. And yes, so it will keep slowly going down over a period of time. So we don't have a particular target or a time line, but it will keep going down over a period of time.

Shailesh Kanani: And sir, in this quarter, what was the impact of ICRR on NIMs, if you can – throw some number on that?

P.N. Vasudevan: The effect of ICRR on NIM. So it was not much. I can give you that the excess deposit we have to place with RBI because of ICRR was about INR180 crores for that short period of time. So that is the effect.

Shailesh Kanani: Okay. Thanks a lot.

P.N. Vasudevan: Thank you.

Moderator: Thank you. Our next question is from the line of Renish from ICICI Securities. Please go ahead.

Renish: Sir, just one question on the ROA. So now given we have already navigated the decline rate cycle with the current NIM. And still we have been able to generate a 2% plus kind of ROA. So now going ahead over the next three quarters to four quarters, when we see margin expansion happening as well as we don't foresee any cost to assets going up materially and the finance cost cycle. So what is our internal assessment on the ROA trajectory over next three quarters to four quarters, sir?

P.N. Vasudevan: See, we are not going to be able to give guidance on ROA for the next few quarters. We don't really want to get into that. But for a long time now, since we became a bank, we have been holding out that as a model, a 2.25% ROA is something that this bank should be able to look at as an optimal returns. So that's something that we have been talking of for a pretty long time. Of course, we didn't deliver it for quite some time.

We have our reasons of demonetization and COVID, whatever. But minus external shocks of that nature, as a business model that we have put in place, which consists of about 15%, 20% of micro finance book and 35%, 40% of small business, 25% of commercial vehicle, etcetera, and from a cost perspective, largely this is a in-house sourced business, we rarely employ DSAs for sourcing our business.

So given that kind of a model and the fact that we have very strong control over our portfolio quality, which we have demonstrated over the last 15 years, if you put all of that together, clearly, we should -- and of course, assuming that we'll continue to strongly invest in terms of technology products and branding over a period of time.

If you put all this together into a model, something like around two quarter is something that one should be able to look at. But we are not saying that we are going to reach that at some point in time. But all I'm saying is that as a model, it should be possible to deliver that kind of return.

Renish: Okay. Okay. Great, sir. And just last thing from my side on the deposit side or necessity on the cost of deposit side. So given this quarter, we have seen pretty sharp increase in the cost of deposits. Is it fair to assume that if rate has to remain where it is right now, the TD cost, by and large, has picked out at current levels?

P.N. Vasudevan: Yes. So I think I mentioned that earlier that we are at 7.21% interest cost for the second half -- I mean, for the second quarter. And most of the old deposits have got matured and repriced. Now I mean we have analyzed our data in terms of how much more of the old deposits are coming up for maturity and repricing in the second half. And based on that calculation, we believe that the interest cost increase should be less than what we have seen in the second quarter. And over the entire second half, we expect that interest cost to go up anywhere in the range of around 25 basis points.

Moderator: Our next question is from the line of Ashlesh Sonje from Kotak Securities. Please go ahead.

Ashlesh Sonje: Hi, Sir. Sir first question is on the PCR front. Do we have any plan, as in what time line are we looking at to take the PCR to 70%?

P.N. Vasudevan: I think we have mentioned that in the previous calls also. We are looking at a two year time frame to reach that level.

Ashlesh Sonje: Okay, sir. Perfect. And sir, secondly, on the capital front, currently we seem to be consuming capital at around 100 to 150 basis points per year. Do we have an internal threshold for the [CRAR] before we raise capital -- equity capital?

P.N. Vasudevan: Yes. So you know that SFBs have a 15% minimum capital adequacy requirement as per RBI norms and which means that at any point, we should not let it go below 18% to be very safe and comfortable. So definitely, 18% will be a trigger level you can say. Second thing is that we have hardly or practically no Tier 2 capital.So what we are likely to look at is that based on the appetite, based on the cost of funds, etcetera, etcetera, we would first look at the Tier 2 option. When our capital adequacy ratio is coming closer to that 19%, 18% level, our first option will be to look at our Tier 2 option. And based on availability, appetite and cost, we'll have to take a look at that. And so raising equity capital in our view, it looks a little different at this point in time.

Moderator: Thank you. May we request you to rejoin the queue, please. Our next question is from the line of Suraj Das from Sundaram Mutual Fund. Please go ahead.

Suraj Das: Yeah. Thanks, sir for the opportunity. Two questions. One, if I look at your segmental asset quality details. So MFI, GNPA and vehicle GNPA is going up. MFI has gone up by around 40 basis points over the last two quarters while vehicle has gone up by around 20 basis points. And this is despite the fact that these portfolios are growing at 40% -- 35%, 40% over the last two quarters. So anything, sir, on ground, what is happening or what you were seeing in terms of asset quality in a couple of these segments?

And also just to add there in the MSE finance, I think your disbursement ticket size has increased from around INR50 lakh to INR75 lakh or so over the last quarter, but the portfolio is degrowing. So what is happening there? Yes. So that would be my first question and I have one more question.

Rohit Phadke: So first, I'll give you the -- answer your first question on what is happening on the ground in various segments. So across -- we see a very strong demand in all these segments in the ground level. And as initially, Vasu sir did explain on the -- all metrics, macroeconomic metrics seem to be doing well. So we see really strong demand for SBL for CVs as well as for microfinance. CVs too, it's very clear. Everything in CV is growing. There is ample availability of loads and freight rates are holding. So there is no dip in demand out there. So there's a very strong demand in all three.

In microfinance, the collections are going very good. X bucket collections have remained stable at about 99.4%, 99.5%. So the industry has been growing at 19.5%, and MFI-NBFCs have grown at 38%. We have grown at 41%. But our guidance continues that we will keep the microfinance book below 20% over the whole -- as far as a proportion of the total advances.

On MSE finance, see, we have had an impact due to COVID. Some of our customers have had an impact. Those customers have not been able to come back very strongly and we are still helping those customers come out of that. It's a very small book. So our intent is that first, we need to get the books clean. The delinquency is pretty high there. So once the delinquency comes in control then obviously, we will grow the book aggressively.

As of now, the increase in disbursements are because the economy is doing well and there is demand there. So we've been able to go to the market, source some good customers and that traction will continue. But if you look at the real aggression will come only when the delinquency in this portfolio has been reduced. Thank you.

Suraj Das: Sure, sir. Okay. Now to there's question more was on the asset quality, the GNPAs in this MFI and vehicles are going up. So any thoughts on asset quality?

Rohit Phadke: No. So seen CVs, usually, it's a cycle. The first six months because of the monsoons, the collection is slightly -- it's tough on CVs in the first six months, and then the next six months, it goes up. But we see very strong collections at the ground level. So there's no need for concern, right?

On microfinance, the delinquencies are not really going up. What has really happened is that -- delinquencies have gone up slightly. So that is not -- I mean it's within the range. So I don't -- so there is no concern out there. It's a range amount.

Suraj Das: Understood, sir. Okay, last question, sir. A couple of...

Moderator: Sorry to interrupt, Mr. Suraj Das. May we request that you return to the question queue for follow-up questions?

Suraj Das: Sure, sir.

Moderator: Thank you. Our next question is from the line of Amit Jain from Axis Capital. Please go ahead.

Amit Jain: Yeah. Hi, sir. Thanks for taking my question and congrats on a good set of numbers. So first question is on -- again, on the segmental GNPA and the small business loans. So it has seen a sharp improvement. So any color here? Why is there some reclassification? Or what has led to the sharp improvement in the GNPA and the small business loans?

P.N. Vasudevan: The ARC sale was entirely the SBL NPA book.

Amit Jain: Okay. And secondly, sir, if you look at the movement of GNPAs, the upgrades and recoveries have been pretty high this quarter. So any color here would be helpful. Sir, any particular segments where we are seeing these recoveries and upgrades?

Sridharan Nanuiyer: The upgrades and recoveries are high because of one is that the ARC sale. So if you look at the recoveries that INR118 crores and we have a written off INR44 crores on that account. So that is the reasoning.

Moderator: Thank you. Mr. Amit Jain, may be the request that you return to the question queue, please.

Amit Jain: Thank you.

Moderator: Our next question is from the line of Abhishek M. from HSBC. Please go ahead.

Abhishek M: Hi, Vasu. Congratulations for the quarter and thanks for taking my question. So can you share some of your plans on branch opening and hiring for the second half?

P.N. Vasudevan: Yes. So I think our branch opening story has been something we have talked about quite often in the past. We have invested quite strongly in our branch network over the last five, seven years after becoming a bank. And we still have a long way to go in terms of ensuring that we are fully leveraging the branch network that we have got.

From the liability perspective, you see, we have nearly 400-odd branches. And so we believe that this is a very strong network of number of branches and it should help us to scale up our deposits to almost double of where we are without any significant increase in the number of branches. We'll keep adding branches year after year but it will not be very strong.

In terms of assets, we have nearly about 500-odd branches where we operate. And one is that there is always a potential to grow further in the existing branches. Second thing is that many of the products are not fully rolled out in all the branches. So there still -- that's still a work in progress where some of the products are getting launched in some of the other existing branches. And that will give us a further ability to grow the book.

So on both ends, if you see, we have a good amount of investments done. And right now, we are really in the process of leveraging that investment. So over the -- I would say, in a time frame of two years, that if you look at a two-year time frame, I guess the number of branches that we will add will not be too much. It will not be very significant.

Abhishek M: Okay. But can you quantify? Or do you have a target where you want to get to which you can say?

P.N. Vasudevan: No, we don't have a target. I mean, see, I guess, last year, I mean I really don't know the number here. But it's not much. Last year, I don't know how many branches we have had, must be in the range of around 20 branches, 30 branches or something like that. And this year, probably it will be in the range of 30 branches, 35 branches or something like that. See, it's not a large number. So I don't even track it very closely.

Abhishek M: Understood. So basically, taking this and your previous commentary about large number of projects getting completed and becoming live, should we expect your opex run rate to be moderate? Like for example, this quarter, it was up some 2.5% Q-o-Q. Incrementally, your opex run rate should not cross your revenue growth for the next three quarters, four quarters at least. And therefore, the jaws should continue to widen, is that a fair assumption?

P.N. Vasudevan: See, the first quarter always, you will have the 10% staff cost hitting us, okay? And staff cost comprises of almost 65% of our total cost. So the first quarter is always going to be kind of negative. And after that, the second quarter onwards, the benefit of income will flow in and open the jaws in a positive manner. That is one thing.

Second thing is that while we are not really looking to invest strongly in terms of branch network, however, we will continue to invest, be it in technology, be it in products. So technology, as I mentioned, we have mentioned a few projects which are completed or underway. And once those are done, there will be -- I'm sure a few more projects that we'll want to take up, which will either improve efficiency or improve customer experience or give better options for the customer to deal with the bank. So those -- I don't think we are going to reach a level where we say the technology investments are over for the -- for us. So that is -- I'm assuming will continue.

Second thing is that our product, we always mentioned that our product investments is something that we continue to invest. So this year, we have taken up two major products, which are our credit cards and the AD1 product. So there's a lot of work going on in that this year, and some amount of expense will be incurred on that this year, but a lot more of expense will be incurred next year. And so the product investment and the technology investment are something which will continue. Branding is something that we will keep kind of moderating or increasing based on what is available in the city. But these two are something that we are fairly committed to.

Moderator: Thank you. Our next question is from the line of Rakesh Kumar from B&K Securities. Please go ahead.

Rakesh Kumar: So excluding this recovery upgrades due to the ARC sale, what would be the normalized net delinquency number going ahead?

P.N. Vasudevan: So our GNPA -- if the ARC sale had not happened, our GNPA was 2.6% in the first quarter. And if the ARC sale has not happened, the GNPA would have remained practically at the same level, 2.5% to 2.6%. So it would remain at a very similar level. So overall, the portfolio quality is very stable. And the sale, of course, helped to reduce the GNPA, but minus that, we would have still been kind of comfortable.

Is that answering you or I didn't quite get your answer of what does that net something you asked me?

Rakesh Kumar: Net delinquency numbers, sir, in Q3, Q4. How would -- that normalized number would be, sir, in Q3, Q4?

P.N. Vasudevan: What? I didn't quite get it.

Rakesh Kumar: Net delinquency numbers, sir. Net delinquency ratio number.

P.N. Vasudevan: What is that? Sorry, I've been in lending for all my life, but I didn't really understand that. Are you talking of NNPA?

Rakesh Kumar: No, sir, basically, your slippage minus recovery upgrade number, sir? Slippage minus recovery upgrade number, how much that number would be in Q3, Q4 on a normalized basis?

P.N. Vasudevan: You are talking of the -- are you talking of the GNPA amount, opening and closing amount? Is that what you're referring to?

Rakesh Kumar: No, so maybe we can take it off-line. No problem, sir. Just a really...

P.N. Vasudevan: I should take it off-line because seriously, I didn't get you.

Rakesh Kumar: No, no problem, sir. No problem, sir. So the second thing, is there any contribution of ARC sale in the interest income line?

Sridharan Nanuiyer: No. The contribution is to the P&L excess provision reverse of INR23 crores, actually.

Moderator: Thank you. Our next question is from the line of Pallavi Deshpande from Sameeksha Capital. Please go ahead.

Pallavi Deshpande: Just wanted to understand on the LCR decline on the liquidity coverage ratio, what would explain that? And how do we see it for doing well? And second one would be on this product development, what would be the cost you're planning to incur for the credit card, sir?

P.N. Vasudevan: Yes. On the product development, as I mentioned, the two major products we are working on in Phase 2. While last year, the previous year, we had launched our affordable housing. So there's some amount of investments going in that. So this year, the affordable housing will break even. And from next year onwards, affordable housing should start contributing positively to the margins.

And the other two new products, credit card and the AD1, that's something which is work in progress. And launch is scheduled for next year. So obviously, next year, these two will drag the bottom line. And hopefully, sometime later, they should start contributing positively.

I'll ask Nat to answer on the LCR part of it.

Natarajan M: What was your question on LCR?

Pallavi Deshpande: We've seen a decline quarter-on-quarter, year-on-year also, 182%. So just wanted to understand the reason and -- of EBITDA and maybe what's the share of wholesale deposits now in the total deposit mix?

Natarajan M: Yes. There are a lot of moving parts in LCR. But the audit description is 600. And internally, most banks have 110%, 120% threshold. You'll agree that our 180% itself is a very healthy LCR. So it's all a function of what kind of deposits we take, where we deploy it. Put it all entirely in H2 obviously, the LCR goes up.

If you want to improve the yield and the park them in non-LCR, which we have done partly, it may not reflect in LCR, but at the same time, liquidity-wise, it's still comfortable. So LCR is just one of the tools to measure liquidity, comfort that a bank enjoys. There are various other ratios as well. So -- but 180%, to answer your query, is quite a comfortable ratio.

Pallavi Deshpande: I agree it's comfortable. I just wanted to understand any wholesale deposits raised in this quarter because the deposit growth was so strong?

Natarajan M: Yes, it keeps coming. Mostly over and above, and focus is on taking Basel-friendly deposits. So as a result of that, our focus will be to -- we'll ensure that most of the deposits are contributing to LCR as well.

Moderator: Thank you. Our next question is from the line of Preet Nagarsheth from Wealth Fin Advisors. Please go ahead.

Preet Nagarsheth: Yes. Actually, my question is regarding the microfinance industry. And there is an RBI regulation that says that the cumulative EMIs of the borrower has to be capped to 50% of the monthly income. Now...

P.N. Vasudevan: Yes? Hello? Can you hear me?

Moderator: Sir, I think the participant has dropped from the Q&A session. We move to the next question.

P.N. Vasudevan: Okay.

Moderator: Our next question is from the line of Arvind R from Sundaram Alterbnates. Please go ahead.

Arvind R: My question would be on the segmental GNPA. So GNPA for SBL alone like actually came down from like -- actually sharply from 3.2% to 1.7 percentage. May I know what is the reason? Like with that ARC sale or...

P.N. Vasudevan: Yes, that's ARC sale.

Arvind R: Okay. And my -- so the recoveries were also like higher. That also came from ARC?

Sridharan Nanuiyer: Yes, recoveries came -- which I mentioned, INR118 crores is the recovery.

Arvind R: Out of?

Sridharan Nanuiyer: Out of INR162 crores of GNPA.

Arvind R: Okay, and one -- just one more question. Like so deposits and term deposits has actually grown by like 80%, whereas retail deposits only grown by like maybe 60%, 58%, I guess. Are we seeing any issue in raising deposits in overall?

Murali Vaidyanathan: Yes. Murali here. No. I think the absolute contribution. See, last year, you're seeing bulk growth because of the low base effect. If you see this year, absolute mobilization, 73%, 74% has come from retail only. So there is no issue in terms of raising retail deposits. In fact, this has been our best retail deposit quarter.

Arvind R: And how confident are we on like getting recoveries in the future quarters also, like do we have a significant recovery pool? Because we are having the 3.5 percentage gross slippage, and if we consider like a 60% PCR, then that still will lead to 2% credit cost. I know like I'm talking only in terms of gross, but what about net level, like how much are you confident about recoveries in the further subsequent quarters also? Like do we have any significant recovery pool?

Dheeraj Mohan: Dheeraj here. So I don't think we should look at recoveries from quarter-to-quarter in that microscopic fashion. And also our gross slippages number is a little different from what others report. So my only suggestion is really don't expect us to give guidance on recovery quarter-on-quarter. I think the overall number we said from a credit cost, keeping how we want to take provisions up, keeping how market cycles are, I think that should be sufficient. I hope you understand.

Moderator: Thank you. Well, 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. So thank you. Thanks all of you for dialing in and giving us a lot of food for thought through your questions. Definitely, we always get educated every time we talk to you people, and we come out with better understanding or more clarity of what's happening around us. So continue to keep questioning us, continue to keep raising your issues and questions with us and help us keep improving all the time. Thank you, and wishing you guys all the very best. Bye-bye.

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