"Equitas Small Finance Bank Limited

Q1 FY '24 Earnings Conference Call"

July 31, 2023

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Moderator: Ladies and gentlemen, good morning, and welcome to the Earnings Conference Call of Equitas Small Finance Bank Limited's Financial Performance for Q1 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 dialling in this morning. The year has started off well, both at the macro level and at the local economy where Equitas operates. The credit momentum continues to be robust and with the early signs of inflation softening, the momentum may continue for the rest of the year. Tractor, three-wheeler sales, vehicle sales and other indicators all point to the right direction and hopefully, monsoon ends well, giving rural and semi-urban economies a boost.

Coming on to Equitas, the bank delivered strong growth across its diversified loan book. We are seeing growth across states. Newer products like commercial vehicles, affordable housing, are maturing well and will start contributing meaningfully to the bottom line soon. We are also working on products like personal loans, car loans, credit cards, forex cards, etcetera, that can be offered to our depositors which can help us improve our overall engagement and stickiness with the depositors. Over the next 12 to 15 months, we hope to see these products rolling out.

On asset quality, things are back to normal with a gross slippage calculated on daily basis. I repeat, calculated on daily basis, hovering around the 3% level and a stable GNPA. Our restructured book is now only about INR213 crores and we have a 97% provision for NPAs arising out of this book and with that I guess the entire restructured issue is completely behind the bank. Rohit will talk in further details about advances.

On the deposit side, the environment is getting tough with most banks increasing their deposit rates. Over the last 15 months, we have narrowed the difference between our peak deposit rate to those of the large banks by about 50 basis points. We were one of the earliest SFBs to focus on CASA, and at one point, we had exceeded 50% CASA ratio. Though this has come down sharply over the last few quarters, yet it remains very good in the banking industry.

We continue to back up our attractive interest rate on savings accounts through high-velocity engagement with depositors through our various channels. We also upped our new CASA acquisition. The story of the quarter for Equitas clearly is our retail TD. We have been able to mobilize almost INR500 crores per month of net accretion to RTD. And channels like NRIs and the virtual RMs are doing quite well to help us deepen our relationship. Murali will take you through more details on this.

While deposit mobilization has been good, our cost of funds has seen an uptick, largely in line with the industry. As you know, more than 80% of our loan book is fixed rate loans, and this had a corresponding impact on NIMs. During the past year, we also increased our lending rates, and our yield on disbursement for the quarter is about 8.4%, which is up 35 basis loans compared to last year's first quarter. However, we feel the changing portfolio mix will continue to put pressure on the NIMs but should be offset to some extent by an improvement in office and credit costs.

Last quarter I mentioned that we delivered a 2%-plus ROI for the second consecutive quarter. Today I'm happy to make that the third. I can never keep my philosophies or my governance standards out of any dialogue. Please indulge me for a couple of more minutes as they ramble along on this. Equitas and ESG. I now want to talk about our approach to customers. As you all know, our borrowers are typically from the informal economy, comprising of the base of the pyramid segment. I repeat base, not the bottom, but the base of the pyramid segment.

Moratorium, where RBI announced a moratorium during wave 1 of COVID, we offered it liberally to our customers and 90% by value and 97% by number of customers availed the moratorium which might probably be the highest among many banks. After that in post two RBI offered a special restructuring window at a time when investors were giving brownie points to those banks who showed the lowest percentage of restructuring, we again offered it liberally to our customers. Outside of microfinance, we restructured about 31,000 customers, of which about 27,000 customers did not move into NPA. This means that if we had not been very empathetic and considerate to our borrowing segment, out of this 27,000 customers, most of them might have slipped to NPA if we had not offered that restructuring, and we would have ended up repossessing their only house property in their life and then brought them to peril.

As I mentioned before, in Equitas, we are not just running a bank. We are running an organization impacting the most vulnerable segments of society and we have to be extra supportive in their times of need and return, they always stand up for us. I believe that these actions of the bank propel us to the highest standards of ESG, benefiting real people in an immediate and direct manner. For all stakeholders associated with Equitas, we not only offer a bank run on high standards of governance, professionalism, and financially attractive, but also a bank which positively impacts large segments of base of pyramid population.

At Equitas, we believe in circle of life. The good you do comes back to you. I repeat, the good you do comes back to you. And so I end this with a big thanks to all of you who have supported us and hope that the circle of life, such as Your Life too, and enlivens it up. Thank you and I now hand it over to Rohit.

Rohit Phadke: Thank you, Vasu Sir and good morning everybody. Advances have grown by 36% and disbursements are 46% year-on-year. Collection efficiencies have been stable and GNP has been maintained at the same level as the previous quarter. In small business loans, there is growth in the non-Tamil Nadu disbursements. In June '22, the composition of disbursements was 65% in Tamil Nadu and 35% in non-Tamil Nadu. At the end of June '23, the composition of disbursements has now changed to 61% in Tamil Nadu and 39% in non-Tamil Nadu. The business has seen growth in the states of Andhra Pradesh, Telangana, Karnataka, and Maharashtra. The new loan registration system has been rolled out and is active in 100 branches across the country. Another 100 branches will go live this quarter.

The microfinance business has recovered from the COVID impact, and X-bucket collection efficiencies are stable at 99.51%. 82% of all customers acquired last quarter were onboarded using e-KYC. 46% of all customers e-signed the agreement, eliminating the use of physical agreements for this set of customers. The vehicle finance business, the used car book has grown and is now 11% of the total vehicle finance advances. The focus is on funding to customers for personal use. The used car market in the country is huge and we aspire to grow this product.

The UCV and new CV portfolio comprise primarily of small commercial vehicles, LCVs, and pickups. In the new small commercial vehicle segment, we have a market share of 10% in Tata Ace in the geographies that we operate. The market share in Ace, those has reached 4.5%. We also aspire to increase the market share in Mahindra Pickup, where we have a market share of 2.3%. The affordable home loan business is scaling up and now operates out of 34 branches in five states. The new LOS for the business will also go live in the coming quarter.

Rural demand is looking up as indicated by various macroeconomic indicators like, rural car and two-wheeler sales. Even FMCG companies have reported improved rural demand. In short, things do augur well for the coming quarter. I'm quite hopeful that the coming quarter will also be good.

Thank you so much. Handing it over to Murali.

Murali Vaidyanathan: Good morning. Bank is actually taking a very sustainable and very scalable effort towards building a very stable and retail-oriented franchise, as we know through differentiated segmental approach and very importantly creating a differentiated channel. I would like to stay put on this for two more minutes.

Our retail deposits, that is our CASA plus RTD, remains at healthy 78%. And that is actually a very healthy sign for two reasons. One, our product holding at the house level and also penetration at the market level for NTB is getting enhanced. Our relationship management structure, where we have put VRM, which is data, voice over data, and then physical RM structure is helping us to grow the RV by 8% to 10% across the spectrum of customers whom we offer. And please note, we also have a VRM based on time zones for the NRI segment.

And now what we are doing through this is, we are actually focusing on family banking as an opportunity. This has helped us our premier program, elite to cross 12,500 crores and very important point today is close to 77,000 families are totally banking with us through this proposition. Glad to see our wings proposition, which we have revamped, focused predominantly towards salaried as a segment, is seeing an encouraging, not only encouraging, seeing a higher penetration of salaried segments coming in towards close to 40% to 42% of the book today of savings account is through salaried as a proposition.

RTD is a very good story, it continues to be. There are two things, one is mobilizing INR1,500 crores, INR1,600 crores net, which means at a gross level, it should be INR2,200 crores to INR2,300 crores. But the reality is we could spread it across to 120,000 customers across the spectrum, both NTB and existing book. So 60% of the existing customers opting for TD inside this enhances our product holding as well as foot on door syndrome. And this will give us an enhanced opportunity.

Our channels which we have dedicated have started giving most productive results. For example, NR, now we are present across 100 countries and the book has crossed INR1,500 crores of RV. So is our institution business, which has crossed INR7,000 crores of RV with 30% of CASA in the industry. So the important segment here, what I want to push on industry businesses, close to 92% of the book is on non-callable deposits. So all these things put together has helped us to maintain a healthy SLR and LCR ratio. And most importantly, we have onboarded 1.3 lakh customers during the first quarter, which means our acquisition rates have gone up.

And second important part is leveraging on physical and digital, our two KYC conversion of digital basis account has gone up. And our engagement based on propensity and analytics model has helped us on debit card activation, and importantly, primary and active accounts reaching closer to 60% mark and our product penetration across DPP is getting enhanced. Our retail and trade focus on current account is helping us to be in top 17 in terms of acquirers and we will continue to monitor our current account and progress there. And overall digital side, I think it's been a very encouraging quarter from prepaid to micro-ATM to full conversion, and we will sustain our journey there.

Thank you, let me hand it over to Gopi on treasury views.

Gopalakrishnan G : Good morning, everyone. Q1 has been largely a steady quarter in the market front. Bond prices improved as yields cooled off with inflation edging down even as the growth outlook consolidated. Past quarters saw RBI passing the interest rate high cycle in April and maintained status quo in June. Despite comments from the RBI Governor emphasizing that the back-to-back pauses by RBI MPC should not be construed as a definitive change in policy direction. There was a cause for optimism that interest rates are nearing their peak on the back of CPI numbers pulling within RBI tolerance ban.

First quarter of the new fiscal witnessed largely positive developments in Indian economy. Stable rupee and macro conditions helped attract strong foreign fund flows into domestic financial markets. Rally in equity markets is primarily driven by steady FDI flows, resilient domestic economy and lower crude oil prices. A few areas of concern continue to hover, mainly uneven monsoon and El Nino, which may have some impact in the inflation. We have seen that bond yields are slightly firming up in July as well, reflecting these developments.

Now, coming to Equitas' Treasury performance for this quarter, this has been another stable performance from Equitas Treasury. Profit on sale of investments stood at INR26 crores. Our funding profile has been stable with opportunities available to raise funds both in the form of refinance as well as IBPC.

Thank you. Now I hand it over to Mr. Sridharan.

Sridharan N: Good morning to everyone. Our net interest income for the quarter came at INR743 crores, as compared to INR581 crores during the same quarter last year, registering a growth of 28% YoY. Other income for the quarter came in at INR150 crores, as compared to INR100 crores during the same quarter last year, registering a growth of 50% resulting in a net income growth of 31% year-on-year. The total operating expenditure came at INR581 crores, as compared to INR412 crores during the same quarter previous year. The increase is on account of annual increments for employees, payout of performance bonus and new recruitment. The bank also invested in the brand by advertisements in IPL.

The cost was accounted for in Q1. Lastly, investments in technology increased as we spent on various IT projects relating to loan systems, customer apps, data warehouse, and other enhancements. This led to a marginal increase in our cost to income to 65.05% for the quarter. Pre-provisioning of profit, PPOP grew 16% year on year to INR312 crores, and PPOP to assets remains healthy at 3.42% for the quarter. PAT for the quarter came at INR191 crores, as against INR97 crores during the same period last year, registering a growth of 97% Y-on-Y. ROA and ROE for Q1 FY24 stood at 2.10% and 14.54% respectively.

As on 30th June 2023, banks restructured loan book stood at INR213 crores, which is equivalent to 0.72% of the gross advance book. NPA on the restructured book was INR160 crores and provision made against this book was, the book stood at INR156 crores. Now moving on to asset quality and provisions. The bank carries a total provision of INR574 crores, NPA provision of INR445 crores, provision on standard assets at INR129 crores. In order to strengthen the PCR, the management made additional provision of INR14 crores and total provision for the quarter is INR60 crores.

GNPA remained flat at 2.6% in Q1 FY24 as compared to Q4 FY23 and improved by 135 bps as compared to Q1 FY23. NNPA came at 1.12% in Q1 FY24 as compared to 1.14% in Q4 FY23 and 2.07% in QY FY23. Provision coverage ratio improved to 57.79%. If ECL is implemented by the bank, the ECL provision will be lower than the IRAC provisioning requirement and to meet the minimum IRAC provisioning requirement, additional provisions will be made as management overlay.

As of June 30, 2023, total CRAR has stood at 22.06% with the Tier 1 at 21.36% and tier two at 0.70%. Lastly, the bank has made investment in setting up its own corporate office building at the heart of the city and we hope to complete the work by early of FY ‘26. With this, I would like to hand over to operator and we'll be happy to take questions from you again. Thank you.

Moderator: Thank you very much.. The first question is from the line of Deepan Narayanan from Trustline PMS. Please go ahead.

Deepan Narayanan: Good morning everyone and thanks a lot for the opportunity and congratulations for good set of numbers. So firstly, we wanted to understand so if RBI holds rate at these levels for a couple of quarters, do we foresee pressure in NIMS continuing or we can pass the rates pressure to our customers fully without affecting growth profile?

Dheeraj Mohan: This is Dheeraj here, Deepen. So as you know, 80% of our book or 80%-85% of our book is largely fixed. So the place where we can actually pass on rates is on incremental disbursements. Incremental disbursements over the years, just for some numbers, have actually got up about 40 basis points. But as you see, our portfolio yields are around 17%, 18%. So that's also – there's limited room for us to expand it, equivalent to how we see rates going up. But still, adjusted for that, to see what impact it will have in the bank, from a – from a yields at a portfolio level, we should be able to hold yields where it is. And also keep in mind that, there is a slight mixed change with housing, new commercial vehicles, a disbursement of the share improving, but we still should hold yields. So one, yes, we have passed on rates to certain segments of the customer. Two, the portfolio mix is playing out well from a long-term cost to assets and credit cost. So we will have that yield passing out being compensated or negated with the portfolio mix. Thirdly, the cost of funds, yes, is moving up. You've seen it spike in Q1. From our estimate, from a cost of funds, is that we may end the year at about 7.5%. This is taking into account where we feel inflation, rates, competition, and deposits, all of that play out.

It will have an impact on NIM, adjusted for all of that. Hopefully for the full year, NIMs should not deteriorate below 8.5%. But if you look at quarter-on-quarter, you may see it go below, especially in the later half of the year, but we still should maintain a NIM for the full year at about 8.5%. This is about a half a percent drop from last year.

Deepan Narayanan: Okay. So our NIM profile should be substantially improved if the rate cycle starts going down, right?

Dheeraj Mohan: Yes, if rates reverses, like we have the bad side when it increases, our portfolio yields will not drop because we don't have floating rate loans. So we should start seeing that benefit play out. But the question is, when it will play out, it's up to everybody's imagination of the industry side.

Deepan Narayanan: And secondly, so now our growth profile has increased substantially. So what kind of cost to income are we expecting for FY '24?

Dheeraj Mohan: So like, what we've been saying, this is actually an investment phase we are going through. We are investing largely in products like credit card, personal loans, the AD-1 license, also will result in a few products being launched. And also in technology, largely on the digital side, Rohit had talked about the loan origination systems, which we are putting in place, which all eventually should help us improve productivity and scale up faster.

And lastly, on the brand, some investments were made on IPL, like Sridharan had mentioned. So we are still in the investment phase. And like we said earlier, the cost to income, this where it is right now, marginally may improve. We've been saying 63% odd. So let's see how it goes. Usually income builds up for us in the second half of the year, so all of that should compensate to where cost of income should remain at let's say 63%, 65%.

Deepan Narayanan: Okay, thanks a lot, I will join back in the queue. Thank you.

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

Renish: Yes, hi, Congrats on a great set of numbers. So just two questions, one again on the deposit rates. So this quarter, we have seen almost 30 basis points in the cost of deposit. So it is fair to assume that, on the blended or let's say the portfolio basis, we are near to peak on the deposit rate side?

Dheeraj Mohan: Renish, Dheeraj here. No, we are not at the peak, like we said. Are you asking on, are we going to introduce any more products with higher rates of interest?

Renish: No, I'm saying, let's say our cost of deposit is at 6.94% and within that we see the TD cost...

Dheeraj Mohan: So, Renish, that will go to 7.5% like I just explained because there will be some deposits getting renewed at a higher interest rate plus our retail term deposit momentum is very strong. So we see that going up to about 7.5%.

Renish: Okay, and that will have a consequent impact on NIM as well, right? For this year?

Dheeraj Mohan: Yes, it will. So I don't know if you heard my previous.

Renish: Okay. I was there.

Dheeraj Mohan: Yes, so it should be somewhere around that. But the NIM, like I said, full year, 8.5%. But you will see NIM go below that, at least in the third quarter and fourth quarter. But hopefully interest income will be also compensated. But NIM, yes, about 8.5% is what we should look at.

Renish: Got it. And just to follow up on that, so when we are delivering this 2% plus ROA as of now, and now, there is some bit of pressure on the NIM. How confident we are that we'll be able to sustain this 2% ROA because we also highlighting that, then the investment fails. So there is no lever on the cost side, credit cost is you know at the best of the level. So how do we sustain this 2% ROA?

P.N. Vasudevan: Yes. So, see the point is that this year, there has to be three, four elements, which we expect to be at play. One is the basic interest income arising out of the growth in the portfolio, which should be one positive support. The second thing is that, we saw the highest increase in terms of percentage from the opex perspective in the first quarter, because typically we do give out the annual increments effective April, so the staff cost goes up sharply between March to April and that obviously will steady up after that and through the rest of the year, the employee cost to some extent except for the new addition of people will remain constant.

Whereas the productivity of those people will start coming in from the second quarters and subsequent quarters onwards. So we should see an opex, which is about 32% increase year-on-year in the first quarter. We expect that to come down as a percentage of growth year-on-year for the subsequent quarters.

So while the NII should go up because of productivity of the staff improving as well as new staff coming in and adding to the business of the bank, the opex should come down as a percentage of growth compared to the first quarter. And the third element at play, we expect during the current year is of course the credit cost. As you know, across the industry, across the banking industry, this is one of the best credit cycles that we are seeing. And even in our own case, we have seen the first quarter was probably the best that we have ever seen in a long time.

Though it is supposed to be a seasonally weak quarter, but actually it was pretty good from a collection perspective. So the credit cost might again come in a little bit from a support perspective. So while these are all the positive factors at play, the negative factors at play for the current year as you mentioned, as Dheeraj mentioned, would be the increase in our interest rates, interest cost from 6.95%, it may go all the way up to 7.5% is what we believe as the old deposits get repriced to the current level of deposit rates.

And NIMs, as Dheeraj mentioned, last year, we had an average NIM of around 9%, and this year we expect it to be averaging for the full year at around 8.5%. So that half a percent NIMs, we should try and meet out by the other positive factors at play, which I just mentioned. So obviously that's a target 2% ROA is something that we would try and focus on. And some of these factors as they play out should hopefully help us meet that.

Renish: Vasu, just sorry to, just rounding back to the same question. So, let's say the productivity or employee cost will remain same or productivity will improve but as we continue to invest towards the franchise build-up, do you see cost-to-income ratio coming down because in opening remarks, you did mention that, the cost-to- income will remain at around 63%-65%.

So how will cost to assets will come down? I mean of course in one part, there will be saving on the employee cost, but at the other part there will be investment going towards the product, some of the, etcetera.

P.N. Vasudevan: Yes, that's right. So the investments as we have mentioned, there are a few areas on which we need to keep investing, which is one on our digital and second is on our products. As I mentioned earlier also, we are introducing new car loans, personal loans, credit cards, and forex cards, and AD-1 products, which will all happen between 12 months to 18 months from today.

But for those products to launch during that time, there's a small amount of working that needs to be done in advance, which will add to some level of investment from the bank side. The only silver lining for the bank is that, we have in the past invested in a very strong network of branches, and so that is one thing that, we'll be riding on for the next maybe couple of years, while we invest in products and digital. We may not have to invest much in terms of physical infrastructure because that's something that we already done in the past. So all put together, yes, so opex growth, as I mentioned from 32% year-on-year in the first quarter should come down over the rest of the three quarters. And cost to income is around 65% in the first quarter. It should marginally come down, maybe 63%, 64%. And when that comes, that's going to be releasing some level of income to the bottom line.

Renish: Okay. Very good, sir. Best of luck.

P.N. Vasudevan: Thank you.

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

Abhishek M: Yes, hi Vasu and team. Good morning and congratulations for the quarter. So two or three quick questions. One, when you say your cost of funds could reach 7.5, you're talking about a full year average, right? Because, or an exit rate for 4Q?

P.N. Vasudevan: We are talking of an exit rate for the fourth quarter, but full year average interest cost could be in the range of 7.25.

Abhishek M: Got it. And in your term deposit, your cost of TD has gone up almost 90 to 100 basis points from the bottom. Is there a lot of repricing that is remaining or do you think, you're pretty much at the end of it?

Murali Vaidyanathan: See, we have done two things on TD. One is, if you up to one year bucket, the rates are in line with what markets are offering. Between 888 days and 444 days, our differential like Vasu sir said in the call, between our cost of funds and other banks cost of funds, we budget 50 basis points. And we are offering a differentiated rates only in these two buckets, for short to medium term saving and medium to long term savers.

So only in these two buckets, which accounts to close to 60% of the book, we are offering more than the peer group by 50 basis points. So the rates are more or less stable. We are not seeing any rate hike to go up unless there is something dramatic happens in the open market.

Abhishek M: Got it. Can you please repeat the 60% of the book is just those two 444 days? And 888 days?

Murali Vaidyanathan: Yes, Correct, so that saves us one long term book. This is for the one short to medium term service who is having a goal based approach. The other one is for slightly longer term who is actually keeping a destination-based approach in his saving.

Abhishek M: Got it. So, 444/888 should reflect current yields, whatever you're offering today. And the remaining 40% may have one part which is at a lower yield, which will get repriced as it matures?

Murali Vaidyanathan: Yes.

Abhishek M: Okay, got it. That's helpful. The second thing is, yes, sorry, you were saying something?

Murali Vaidyanathan: Yes, go ahead.

Abhishek M: Yes. So the second thing is, on slippage rates, now you're at 3.3%. If you look back before COVID annualized, so if you look back before COVID, you were ballpark at 3.5% plus minus, obviously good times, bad times, but 2.5%, 3.5%. So do you think these should sustain here or go down? And correspondingly, your credit costs, last year average was about 1.5%, 1.6%. This year, you've started at 0.84%. Do you think, this should definitely remain below 100 bps for the year?

P.N. Vasudevan: Pre-COVID, yes, our gross slippage used to be around 3.5%, and during peak COVID, it had crossed to 5%, so around 5.5% to even 6%. Now it's come down to 3%, but there is one crucial difference. Pre-COVID, are reporting gross slippage based on month and figure, which means that, during the month if someone slips into NPA and then, pays back in full and stops being an NPA within the month, it was not getting, calculated for gross slippage, which we changed.

And we had informed this, about four quarters or so back. We had informed that, we have changed it to daily. So that way, the pre-COVID, 3.5% is actually not very comparable to the current quarter of 3%. And to that extent, I believe that, even our portfolio quality are actually further improved compared to even pre-COVID to that extent, And the second thing is from a credit cost perspective is last year, we had a credit cost of around 1.55% and this year, we have guided for 1.25%. And we'll have to keep our fingers crossed. And I believe that, we are in for a good credit cycle, as I mentioned earlier. And let's see how the whole collection goes and hopefully, we should be in for some good collection performance for the current year. But parallelly, our PCR is around 58%. And so there is obviously some aspirations from our side on the PCR to also try and increase it over a period of time. So that might come in for some level of credit cost, if not necessarily from just the normal provisioning. But we might do some extra provisioning only from the perspective of moving the PCR up.

Abhishek M: Vasu, any target for this PCR? Because, in case there's, more than expected NIM pressure, can you push it out? Because the PCR is already at a reasonably good level.

P.N. Vasudevan: Yes, our destination PCR is the standard, typical 70% which most banks are. So that's our destination PCR and we have been looking at it to try and take it to that level over the next few quarters. So we'll have to just take it over the next few quarters to move it to that 70% level.

Abhishek M: Got it, Vasu. Thank you so much and all the best.

P.N. Vasudevan: Thank you.

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

Deepak Poddar: Hello. Yes. Just thank you very much, sir, for the opportunity. So first up, just a clarification. I mean, PCR to 70%. So that effectively means some INR90 crores to INR100 crores of additional provisioning, right? So that we expect to come in the remaining three quarters, right? Apart from your standard provisioning that we have been doing.

P.N. Vasudevan: Not necessarily. We are looking to take it to the 70% level over the next two years. So that means the balance may be seven quarters or so. That's what we are broadly looking at. These are not something hard cast or, casting stone, but broadly that's what we are looking at.

Deepak Poddar: Understood. And sir, in terms of your percentage of portfolio, which has not been repriced as of now, so how much would that percentage be?

P.N. Vasudevan: See, our fixed rate loan book is approximately around 83%, 84%. The balance is floating rate.

Deepak Poddar: So 83% of portfolios is not yet, I mean...

P.N. Vasudevan: They won't get repriced, they are fixed rate loans. So they will earn at the same level of interest rate.

Deepak Poddar: Understood. And what will be the tenure?

P.N. Vasudevan: In our scenario, typically what happens is in a rising interest rate scenario like currently, so naturally, we will have the negative impact of it and hopefully somewhere down the line, when the interest rate cycle changes, that could be the opposite effect for the bank.

Deepak Poddar: I understood. And what would be the average tenure of that 83%?

P.N. Vasudevan: Gopi?

Gopalakrishnan G: Yes, the average maturity of assets is around two and a half years.

Deepak Poddar: Two and a half years, fair enough, I understood. And sir, I also wanted to understand in terms of liquidity, do we hold any kind of surplus liquidity, which is having a negative carry on our NIMs or on our spreads?

Gopalakrishnan G: Yes, so the liquidity per se, we do continue to maintain the liquidity which is adequate to meet our focused funding requirements and yes, and it is LCR is, we also maintain a higher level of LCR if you have seen from the numbers, so the number of LCR for the June stood at around 200% around close to 240%.

Deepak Poddar: Yes, so any thought process to reduce that, if it is having a negative carry on our P&L?

Murali Vaidyanathan: See, LCR is a byproduct of quality of deposits. While our SLR stands at 18% to 18.5%, we are able to maintain higher LCR because of the quality of deposits. So since the quality of deposit is predominantly individual and retail skewed, this is having this impact. And it will have an impact of 30 bps, 40 bps.

Deepak Poddar: So it will continue, right?

Murali Vaidyanathan: Yes, it will continue.

Deepak Poddar: Understood. And, sir, in terms of cost to income, you mentioned about this year, but if I have to see over the next two years to three years, how do we see cost to income panning out?

Dheeraj Mohan: Yes, so from a cost to income, we see the next two years as an investment phase, but obviously these return ratios will improve. So cost to income, at least in our forecast, next year should be a lot more palatable. It should be hopefully somewhere around 60% or below. And from a medium term, we've always been saying that, it should be between 55% to 60%. And that's how the model works. Exceptional modeled for Equitas. So we don't see cost income going below 55%. And in investment phase, it will be between 60% to 65%. So it should taper next year. And the year after that, it should be at least where the model is.

Deepak Poddar: I understood. That's very clear, sir. And that's it from my side and all the very best. Thank you so much.

Dheeraj Mohan: Thank you.

Moderator: Thank you. The next question is from the line of Nitin Agarwal from Motilal Oswal. Please go ahead.

Nitin Agarwal: Hi. Good morning. Congrats on good set of numbers. So, sir, one question on the liability franchise. While we have been reporting a very healthy CASA run rate, but the savings from the peak has come down by 13%. And so when you now look at a cost of fund going up to 7.5%, what sort of further CASA decline are you building in?

Murali Vaidyanathan: See presently, if you see cost of funds, it has three components CA, which is zero cost,SA which is at 6.18%,which is actually lower than last year. This shows two things One is book that has moved into TD so it is having a TD cost here. Second up to 5 lakh bucket our average cost is only closer to 4.8, 4.7 that book has expanded also. So, which means a spender is building balance, a saver is moving the bucket from savings account to TD, and rightfully so.So, we are looking at our pole that is retail pool of liabilities as a strategy. Adding more consumers into retail is very key at this point of time. So, we see a temporarily 1%, 2% dipping down and then stabilizing and we taking it up. So, what this has gained to us at this point of time is we have incrementally added 1.5 lakh more customers whose product holding has gone beyond 2. So, that is why we are saying that incremental TD cost will be ranging 7.6 and 7.7 Savings account will be moving at by 7 basis point to 8 basis points and overall the cost being coming to 7.5.

Nitin Aggarwal Right, okay, and CASA sustaining 35 plus?

Murali Vaidyanathan: Yes, 35 plus should be our ambition.

Nitin Aggarwal: Right, and the other question is on the MSE finance that has been a segment which we have not been growing. There has been a Y-o-Y decline. But if I look at the average ticket size in that segment, that is still higher versus what it was in the last quarter. So, with the unwinding that is going on, on a Y-o-Y basis, so why is the ATMs going up and how do you look at this segment when it comes to the growth going forward?

P.N. Vasudevan: Yes, the MSE is contributing about 5% of the book now and so that's one product where we are basically keeping it as part of the bank bouquet of offerings to meet the working capital needs of the micro-entrepreneurs. We are really not even in the small and medium. We are really in the micro part of the MSME segment. And if you see the data that we have put out, the NPA in that particular segment actually is on a higher side level also.

So, that is an area where some amount of changes was done sometime about 2 years, 2.5 years back in terms of the credit filters and the LTV norms. And so the book that has been being built over the last 2 years, 2.5 years has a much better quality. And so somewhere down the line we expect that NPA to come back to a more normal levels and then you will see that this portfolio should start growing at a rate which is more or less in line with the rest of the bank products.

Nitin Aggarwal: Sure sir. Thank you so much.

P.N. Vasudevan: Thank you.

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

Ashlesh Sonje: Hello, hi team. Good morning. A few questions from my side. Firstly, on the CD ratio, we have indicated that we want to bring it in line with some of the larger banks. So, what is the target here? What is the horizon over which we want to meet this and what does this mean for the deposit growth outlook that we have?

P.N. Vasudevan: So, on the CD ratio, there is no hard and fast norm that we have put in place. It's something that is more directional and operational that we want to do over the next maybe couple of years or so. So, currently our CD ratio, including the refinance that we get from institutions is about 95% or so. And so we would like that to come down to maybe about 85% or so over the next couple of years or broadly in that range.

Ashlesh Sonje: Okay, perfect. And secondly, if I look at the granularity of deposits, that seems to have worsened a little bit. If I look at the proportion of deposits held by individuals that has declined, even in the SA and TD deposit breakups, which we have given, there is a clear shift from lower ticket deposits to higher ticket deposits. So, what exactly is happening here and when do we expect this shift to stop happening?

Murali Vaidyanathan: See, at a portfolio level, 78% is retail and 22% is we call it bulk. Within the bulk, today we are having an institution opportunity to build a stable, non-callable deposit base with a tenure of one year. So, that is helping us to garner two things. One is to get the pool of money in, and second, through that, we are also getting the transaction-centric accounts of them. So, this will continue to be in this direction, where 75-25 will happen very soon.

So, our direction is we'll continue to build granular accounts, 5%, 10% LCR centric accounts, keeping the focus of product holding at a retail level. And as and when the insti opportunity comes in, we will start getting it into it. So, these are all the institutions which we are taking it in it, which is the non-callable base and most importantly, the institution which is giving us the duration. So, this will continue to grow in this direction. So if you see 1 lakh to 5 lakh, if you are predominantly what I said, spenders as a segment is close to 18% which has gone up compared to last year.

Ashlesh Sonje: Okay, perfect. Just one follow up on that one. The NiyoX deposit base which we have, amount of deposits there seems to be, and the growth there seems to be quite weak, any plans to ramp that up?

Murali Vaidyanathan: Yes, see total our book is close to INR1, 200 crores at this point of time, as we speak from a digital segment. Niyo now what we are doing as a conscious activity is no longer called an Equitas Savings Account only. We have deputed a dedicated VRM channel and a specific engagement platform through which we'll engage and deepen the customers going forward. So, you will see a traction in line with Selfe as a product. So, Equitas has Selfe and Equitas has NiyoX. So, both are digital combo product. One caters to the geographical concentration, that is where our branches are there. We focus those customers.

So, Selfe is predominantly geographic-centric. Niyo is demographic-centric. So, Selfe, the biggest advantage is, since it's a geographical-centric, consumers are preferring branch being a closer vicinity. Now that we have engaged a VRM channel to get NiyoX, it will continue to sustain the growth.

Ashlesh Sonje: Okay, perfect sir, thank you.

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

Nidhesh: Thanks for the opportunity, sir. Sir, on the IPL branding, can you quantify the cost that we incurred in Q1 that is first question. And secondly, on the productivity after implementing LOS in the vehicle finance, can you quantify what is the improvement in productivity or any other benefits which can be quantified after this rollout and what can we expect to improve -- productivity to improve in the other segments where we are rolling out LOS in this current year?

Sridharan N: The first question on the IPL costs is INR7.5 crores.

Rohit Phadke: So, on the benefits of LOS implementation, how the productivity will improve is one, the LOS will create a completely paperless transaction. So, from when we implement e-KYC to eSign, there will be no paper involved. We can onboard the customer easily onto the app and straight away going to disbursement. So, you will see the productivity in terms of one, number of files per person that he can onboard. Number two, the number of backend people we need, lesser number of people to process the files. So, once all the LOS gets into full implementation, we can see these productivity benefits.

Nidhesh: In vehicle finance, I think it has already been implemented. So have you seen any?

Rohit Phadke: In vehicle finance, 92% of all disbursements are currently in HETRA, but there is still 8% of functions to be implemented. In vehicle finance, you're already seeing the productivity go up because we have not added many people there, but the volumes in vehicle finance have grown. You see a 39% growth in advance in vehicle finance.

Nidhesh: Okay, so that has happened without the addition of employees?

Rohit Phadke: Absolutely, very less people we have added.

Nidhesh: Okay, thank you, sir, that's it from my side.

Moderator: Thank you. The next question is from the line of Darpin Shah from Haitong India. Please go ahead.

Darpin Shah: So most of the questions have been answered. Just one thing on my part is, actually sir on the TV interview, you mentioned that slippages will still be around 3%, if things are looking better on ground, we are growing at a faster rate. So, why then still have a 3% kind of guidance or for slippages?

Dheeraj Mohan: Yes, so see those gross slippages, I don't know with which number you have to compare because what we have seen is not too many institutions put out gross slippages which can be comparable. So, which is why we keep saying 3% is the healthy run rate which we have and it should remain steady at this level.

Darpin Shah: My point was in first quarter also we are roughly at around 3%.

Dheeraj Mohan: Correct.

Darpin Shah: Which is a seasonally weak – which is a seasonally weak quarter, so when things get better, in terms of seasonality for 2Q, 3Q, 4Q?

Dheeraj Mohan: Yes sorry for a seasonality Q4 actually you will see it improving much better, but like what we said that we are in a good credit cycle. So, assuming a 3% slippage for the full year is not too off. And if Q4 typically plays the way it plays every year, it will obviously be below 3%.

Darpin Shah: Okay, fine. That’s it. Thanks a lot.

Dheeraj Mohan: Thank you.

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

Shreepal Doshi: Hi, sir. Thank you for giving me the opportunity. The question was pertaining to the MSE segment wherein, if you look at the GNPA have only been going up. So, I mean, whereas if you look at the share is not so significant, but the GNPA in that segment has been going up. So, could you please throw some light, what's the reason and what's the reason for this particular product?

Rohit Phadke: So, these are basically overdrafts and term loans given to MSME customers over a period of time. See, during COVID, a lot of MSME customers got infected, and some of them have still not come out. So, that is why the GNPAs are still high here, because they're all collateralized and there is property. So, it takes time for us to proceed legally against them and neutralize the property. But you will see some decent reduction in GNPAs this year. We are all aspiring for that.

Shreepal Doshi: The ticket size here is also like 48, lakh, 50 lakhs at the time of disbursements, so are we able to invoke SARFAESI in these cases?

Rohit Phadke: Yes, we are able to invoke SARFAESI as all of these are backed by collateral.

Shreepal Doshi: Okay, got it. And so to Vasu sir, what's the update on the universal banking license, any timeline for that?

P. N. Vasudevan: As we have mentioned before that merger was one licensing condition and now that is behind us, so technically we have now completed all our licensing conditions. So, now we have to just wait somewhere down the line, we assume that the regulator will probably come with some kind of a guideline on who can apply for converting from SFB segment to universal bank. So, some kind of a guideline probably will emerge from the regulator and as and when that comes, then we'll have to see whether we comply with those requirements under those guidelines and if we do comply, then we'll be in a position to apply. So, there is no particular timeline that we have in mind. We have to just wait and take it as it comes.

Shreepal Doshi: Okay. So this question was on the back of our thought process to launch new car, personal loan, credit cards. So, then say products like credit card would be a tie-up product only broadly. Is that a fair understanding then?

P.N. Vasudevan: What tied-up product?

Shreepal Doshi: Yes, like with some other banker or…

P.N. Vasudevan: No. See the new car loans that we will be launching during the current financial year is largely a product that will be targeted for the deposit customers and our own asset customers. There will be largely a cross-sell product to the existing customers. So, that's not an area where we will be seeking to go to the market and acquire open market customers through the dealership, where the kind of commission payable etcetera makes it really unviable for someone like us.

So, that will be lastly a product that will be targeted only for cross-sell to the existing customers, essentially the deposit customers and some of the asset customers. In the deposit side, we already taken out certain data. We have a few lakh customers whose credit bureau score is over 750. So, those kind of segments is what we'll really be looking to cross sell a product like new cars. And Nano's car the dealer commission because it will be direct to customer. So, hopefully it will be a viable product for the banks.

As far as credit card is concerned, I think we have mentioned in the last time also that something that we are working on and we will be launching our own credit card, but that we expect it to happen only around maybe a year plus from today. So, there will be some amount of cost we may incur in terms of setting up the system. But over a year's time we hope to launch it subsequently.

Shreepal Doshi: Got it sir. Thank you so much and good luck for the next quarter.

P.N. Vasudevan: Thank you.

Moderator: Thank you. The next question is from the line of Harsh Shah from Dimensional Securities. Please go ahead.

Harsh Shah: Hi, sir. Good afternoon. My first question is on the opex and the digital services. If I look at last quarter's, our employee cost has almost increased from INR90 crores to INR330 crores that we are spending today. We have spent around Rs 30 Cr in digital spend while loan also increased to the same extent. So, why are we not yet seeing the impact of productivity that we're speaking of because we already spent almost INR400 crores in technology in last 12 quarter itself?

Dheeraj Mohan: See some of these technology costs will take time to actually start showing from a P&L benefit, but just to add on to also what we were asked earlier in terms of productivity benefits you really look at disbursements for employee last year to this year, from roughly about 18% is actually moved up to about 22, sorry, 18 lakhs is moved up to about 22 lakhs. And some of these benefits can be directly attributed to loan origination system being put out, especially for vehicle finance, where the tax for disbursements are much, much faster than what it was historically.

And again, some of the other investments in technology is really from a scaling up perspective. So, two years, three years from now, from a backend perspective, and those are investments in cloud, investments in APIs or Microservices, investments in platforms like Microsoft Dynamics, etcetera. All of these will actually give you benefits only after a couple of years, but it will help the bank really scale up, which is why we are saying that this year and next year, you may see that not positively adding to the P&L, but after that, you should start seeing some of those investments pay off.

Harsh Shah: Okay. And given that the tenure of our loan is at around 2.5 years, what is the thought process of doing most of the lending at fixed rate and not 2.5 years is fairly long period to have some sort of interest rate risk. So, just wanted to understand the thought process there and incrementally what is the ratio between fixed and floating?

Rohit Phadke: So we have already, Vasu sir has already said that fixed rate loans are at about 83%. Secondly, this whole thing about fixed and floating, it also depends on the product. For instance, you can't do vehicle loans at floating. You have to do them at fixed because that's how the industry operates whereas home loans, yes, home loans we are doing at floating rates. So, it depends on which product that you're lending. So, your fixed and floating will depend on that.

Harsh Shah: Okay, and last question, just a bookkeeping one, the fee income, if I look at it as a percentage of disbursement has come up from 1.5% to 3%. The last quarter it was around 1.5%, it has come up from 25 bps. So, is it just one off or any?

Dheeraj Mohan: Yes, so about 70% of our fee income is linked to disbursements, which are processing fee and login in fee, etcetera, that has actually remained healthy quarter-on-quarter. If you compare with the last quarter of the year, there were, I think we did some disbursements in NBFC loans, etcetera, which is why the percentage may be looking skewed. But otherwise, the processing fee and of disbursement link fee has remained healthy at about 70%.

Harsh Shah: Okay. Thank you so much.

Moderator: Thank you. We take the next question from the line of Pritesh Bumb from DAM Capital. Please go ahead.

Pritesh Bumb: Hi, sir. Good afternoon. One question was on recoveries. How do we see recoveries going ahead? Is the pool now getting lower and lower and is it going to the hard buckets? Is there some sense on the recovery and upgrade, it has been lower this quarter?

Dheeraj Mohan: Yes, so recovery has been lower this quarter just from – to give you a number. Last year roughly about INR36 crores was the income which we got from recovery and that pool actually has come down. So, this quarter, it is about INR3 odd crores. Yes, so this line item will start coming down.

Pritesh Bumb: So, actually, I was talking about the GNPA movement recovery basically, not the written off recovery?

Dheeraj Mohan: It is upgrades.

Pritesh Bumb: Yes, the recovery upgrades, yes.

Dheeraj Mohan: Yes, the pool actually has come down. If you look at it, the opening NPA numbers have come down from 861, it's come to 723. So, correspondingly, you will see the upgrade come down. It will also build up as the year goes by. So, this is only the first quarter. So, recoveries will from the pool will happen.

Pritesh Bumb: Sure, so why I was making a sentence because you report on a daily basis, the NPA. So, you said that 3% is a normalized capacity will come in. But what we've not seen is that the recovery not coming through this quarter at least, that's where the question basically and the second question was on the PCR Vasu sir mentioned it to be moving on a normalized basis to 70. But what will be the triggers to increase the PCR voluntarily or any triggers, because asset quality cycle is benign and your secured book does not require that kind of a provisioning, but what will trigger it to move up towards at least 65% sometime from now?

P.N. Vasudevan: It's more of general prudence, really. And just going back to your previous question in terms of the recoveries and upgrades, if you look at it, last year first quarter, this is on page number 20 last year first quarter the recovery and upgrades were 51.75 and 95.64. If you add that and take it as a percentage of the opening GNPA it's about 18% and this year first quarter similarly if you think 87.38 and 49.38 and sum it up divided by the opening GNPA that is 723.96 again it's 18%.

So, broadly what happens is the first quarter, whatever the seasonality that one typically experiences, the first quarter has been quite in line with what are the similar upgrades and recoveries of the first quarter of last year and hopefully and it was a higher, I mean lower level of gross slippage. So, I think it's a good combination that we had a lower level of gross slippage, but an upgrade which is practically in line with the last year's first quarter. And hopefully as the collection seasonality picks up, which happens typically after the first quarter, we should hope to see an even better upgrade and recovery going forward.

Pritesh Bumb: Sure. Thank you so much.

Moderator: Thank you so much. 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 his closing comments. Thank you and over to you, sir.

P.N. Vasudevan: Yes, thank you. Thanks, all of you. Thanks for dialing in and giving us a lot of food for thought through your questions. And we shall continue to work to try and create the best retail franchise for the banks in the informal economy sector of the country. There is a large unmet demand as we keep mentioning and we do hope that we will be a banker of choice for those millions of people in that base of the pyramid segment and looking forward to all your support on an ongoing basis. Thank you so much. Bye-bye.

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