Poonawalla Fincorp Limited

"Q3 FY 2023-24 Results Conference Call"

January 18, 2024

MANAGEMENT: **MR. ABHAY BHUTADA – MANAGING DIRECTOR**
MR. SUNIL SAMDANI – EXECUTIVE DIRECTOR
MR. HIREN SHAH – HEAD, STRATEGY, BIU & INVESTOR RELATIONS

Moderator: Ladies and gentlemen, good day and welcome to the Poonawalla Fincorp Q3 FY 2023-24 Results Conference Call.

Please note that this conference is being recorded. I will now hand it over to Mr. Hiren Shah. Thank you and over to you, sir.

Hiren Shah: Thank you, Manav. Good evening, everyone, and thanks for joining this conference call. It is our pleasure to welcome you all to discuss Poonawalla Fincorp's business and financial performance for the quarter ending December 31st, 2023.

To discuss all these in detail, I have got with me, our Managing Director – Mr. Abhay Bhutada, our Executive Director – Mr. Sunil Samdani, other senior management officials and myself, Hiren Shah – Head of Strategy, BIU, and Investor Relations.

Now, I would like to request our Managing Director, Mr. Abhay Bhutada, to brief you all about the Company's Operational and Financial Performance, along with the development for the quarter ending December 31st, 2023. Over to you, sir.

Abhay Bhutada: Thank you, Hiren. Good evening, everyone.

I welcome you all to today's earning call and hope you are doing great.

As I give a snapshot of our performance and highlights for the quarter gone by, I will first start with a quick macroeconomic update**.**

In Q2FY24, our real GDP growth was at 7.6% YoY which was better than expected. The Reserve Bank of India has projected a sequential slowdown in the GDP growth in the remaining two quarters and expects the overall FY24 GDP to come around 7%. This needs to be looked at with the backdrop of the fact that the economy grew by 7.2% in the last fiscal and the government had estimated a growth of 6.5% for the current fiscal. However, higher than anticipated growth in the first two quarters of the fiscal has given more confidence in economic prospects, implying that the economy is doing well.

At the same time, the CPI inflation stood at 5.5% approximately, while the interest rates continued to remain firm over the last two quarters. While global growth is expected to be slow, India's GDP growth is expected to be around 7% in FY24 and around 6.5% in FY25. India stands out on GDP growth outlook, driven by renewed CAPEX cycle, well capitalized banking system, robust credit growth, upturn in real estate sector, robust domestic consumption, and growing exports. India has been the fastest growing large economy globally over the last two years. This represents an opportunity for us as we expect this to get translated into steady credit demand from both MSME as well as consumer segment. Our efforts to build a strong and sustainable organization position us best to leverage this opportunity and, in the process, enables the dreams of our customers.

The opportunity is further amplified with favorable demographics, increased focus of the government on digitization, growing disposable income level with a mass middle income population, ever-growing high-income population, government push for infrastructure and growing aspiration of all the Indians.

Now coming to our performance, as we enter the last quarter of FY24, I must say the previous three quarters have been phenomenal for us, not just in terms of what we have achieved so far, but also as to how we have made ourselves ‘future-ready’. The ‘mix of now with the balance of next’ will ensure that we will continue to be a thought leader with extraordinary execution capabilities.

I'm happy to share that we have recorded the highest ever quarterly disbursements, strong growth in AUM along with best-in-class asset quality, resulting in the highest ever quarterly PAT yet again. Again, quarter-on-quarter we are achieving the highest ever numbers.

Now, let me take you through the key financial numbers for the quarter.

We reported our highest ever quarterly disbursements of ₹ 8,731 crore which is up by 159% YoY and 12% QoQ. During the last quarter, we started scaling up instant personal loan through our cutting-edge mobile app, a step forward in shaping the financial landscape. Talking of assets under management, which stood at ₹ 21,946 crore, reflecting a growth of 58% YoY and 9% QoQ.

As regards the composition of our total AUM, MSME constitutes about 42% of our book followed by loan against property at 17%, personal and consumer finance at 16% and pre-owned car contributes 14%.

The secured to unsecured book stood at 52% and 48% respectively. The secured book is growing at a steady rate as disbursements in LAP, POC and MSME continue to grow. With longer tenure LAP book, we expect our secured book to continue to grow. Our guidance on the secured to unsecured mix will be 50% each in the medium to long term. With the change in risk weights as guided by the regulator, we remain adequately capitalized with a capital adequacy of 38.2% as of Q3FY24.

On the tenure mix of our book, the short tenure loans up to 12 months tenor stood at 22% of the book, fairly in line with guidance of 20% to 25%. Similarly, the medium to long term loans of more than 12 months are at 78%. Again, this is in line with our guidance of 75% to 80%. The ideal tenure mix is helping us to improve our profitability while keeping the AUM growth in place. We continue to be a national player with presence across 19 states, having a branch network of 103 branches. The portfolio continues to grow across all our products, and we have a well-diversified geographic distribution with no large market concentration. Our portfolio is also well diversified across both MSME and consumer segment.

Asset quality continues to be the best-in-class and in line with our guidance. Gross NPA stands at 1.33%, down by 36 bps YoY and 3 bps QoQ. While net NPA is at 0.7, down by 19 bps YoY and 2 bps QoQ as we build our portfolio with high resilience. The asset quality is reflective of our approach of having the right of selection. Our Provision Coverage Ratio (PCR) stood at 47.3%.

We continue to optimize our cost of borrowing further and it stood flat at 7.99% for Q3FY24 as against 7.98% in Q2FY24. We have been able to manage our cost of borrowing well despite tight liquidity condition and hardening of rates.

Our NIM stood healthy at 11.02% during the quarter. This is in line with our guidance of steady state NIM of 10% as we continue to focus on high credit quality customers.

Our operating efficiencies continued to improve further. The OPEX to AUM ratio stood at 4%, an improvement of 206 bps YoY and 18 bps QoQ. The reduction in OPEX ratio signifies the productivity enhancement that has been achieved. As we grow, these ratio should continue to optimize further.

The interplay of all the above is reflected in superior profitability. The Operating Profit for the quarter was ₹ 350 crore, which is up by 125% YoY and 4% QoQ. Profit After Tax for the quarter stood at ₹ 265 crore, which is up by 76% YoY and 15% QoQ excluding the impact of exceptional items. Our Return on Assets was at 5.3% for Q3FY24, which is up 84 bps YoY and up by 34 bps QoQ.

Moving on to the business strategy,

It is well carved out and aligned to our stated vision of 2025, articulated at the time of acquisition along with a strategic road map of “Consolidate, Grow and Lead”. The clarity of strategy and its execution is one of the biggest differentiators for us. We have remained true to it and are now bearing the fruit of the same.

Our strategic focus has been on;

- our chosen segments of consumer and MSME,
- prime bureau tested customers having lower credit risk, and
- our PTCS model, i.e., optimum pricing, best turnaround time, convenience, and excellence in customer service,
- building a branch like digital driven model,
- going deep in urban and semi-urban markets,
- focus on risk adjusted returns delivery and not just spreads,
- leveraging technology for operational efficiencies,
- understanding the ever evolving customer behavior,
- being fair and trustworthy.

India's overall credit is growing at a pace of ~10-12% CAGR with consumer and MSME growing at ~20%. The credit demand is led by robust economic growth, increasing per capita income, rising smartphone & internet access, higher employment, and availability of large segment of the population still underserved or unserved. As per TransUnion, more than 160 million Indians are credit underserved whereas around 50% of India's population, ~700 million are credit unserved with no credit history. CIBIL report highlights that out of 220 million credit eligible retail customers, only 33% are being serviced by banks. The same is evident from credit card penetration, there are approximately 66 million outstanding credit cards versus 892 million outstanding debit cards.

Owing to the rapid adoption of digital platform and devices among the younger population in the country, fintech NBFC lending to young borrowers has surged by 100x between 2015 and 2021. The Indian digital consumer lending market is projected to surpass $720 billion by 2030, representing nearly 55% of India's total $1.3 trillion digital lending market opportunity. Thus, there is ample growth opportunity for India's financial sector in the near foreseeable future.

As per the bureau records, the retail loan book has almost doubled in the last five years with growth led by unsecured loans. Digital platforms have been active in catering to consumption needs through personal and consumer loan. High focus on consumption lending empowered them to scale faster.

Now with the regulatory changes, there is a large opportunity for lenders who have the capital and technology available, right risk management capability, and fair customer practices to address and serve this segment. One must note that prime and above prime customers constituted 33% of the disbursement through digital platform as per the bureau records.

We, in our Small Ticket Personal Loan segment follow a stringent approach and only lend to customers who are within our risk asset acceptance criteria. Our risk acceptance includes ticket size of more than ₹ 50,000, bureau score of more than 700, fully digitally verified KYC along with mandatory Aadhaar linked to mobile.

Given the adoption of technology in the small loan segment, digital penetration is likely to go up in the higher ticket size segments as well. With the digital trail of data and technological advancement, interconnected system and platform, widespread use of Aadhaar, PAN, GST, open APIs, automation, etc. the digital contribution across segments will continue to increase and we believe our distribution must be aligned to the same. We are building a distribution system that addresses the same and is aligned to it.

We continue to be invested across all sales distribution channels. We look at the efficiencies in terms of cost of acquisition to be the core determinant of our channel mix. We now have omni-channel presence across Web, App, WhatsApp, Contact Center, Branch as well as channels. This omni-channel presence helps us to use the right delivery channel for each product, thereby having a multi-dimensional play.

Our web presence has increased multifold and now it is getting complemented by both PFL App and WhatsApp. These digital channels have shown high effectiveness for unsecured loans. We are now working on leveraging this channel for secured products as well. We have been able to increase our digital business contribution in pre-owned cars to more than 10%. We are now focusing on building the same across our other secured products including LAP. With app gaining traction, we will have higher direct engagement with our customers across the loan life cycle. This would help us penetrate deeper into the digital lending ecosystem, drive active engagement, meet not only their borrowing needs but also other financial product requirements, going forward, thereby providing significant opportunities to cross sell and upsell.

Organic distribution is something that is strategic to us, and in line with that we scaled up our mobile application distribution in Q3 and customers are actively engaging for both loans as well as service through this channel.

Sales productivity is the biggest efficiency measure, and we track it very closely. Over the last six months, it has increased significantly through various interventions on technology, process, people, and product aspect. We have created attractive incentive and career growth plan for high performers and have refined our products to ensure sales effectiveness without compromising on the risk. We are pushing the bar here continuously and is reflected in the transformation metrics getting better by creating enablers for employees to deliver the same.

On our existing products, we continue to increase our market penetration. We clocked the highest quarterly run rate in our LAP business during this quarter. We have crossed ₹350 crore monthly run rate in LAP. We also achieved our highest ever monthly numbers in pre-owned car loans as well as in business loans. We are a significant player in the PoC market. Now we estimate our wallet share on a monthly disbursement basis to be between 4% to 5%. Our direct Small Ticket Personal Loan product driven through app continues to gain momentum.

Last quarter, we also received approval for co-branded credit card launch. This will be a complementary product for our existing product basket as it helps us engage with the customers in their day-to-day transaction. With the increased penetration of digital payments, co-branded credit card will make us an active participant in the payments ecosystem. It also provides a sizable opportunity to market another product to our existing and ever-increasing customer base, enhancing our cross-sell opportunity. We expect the co-branded credit card to go live this quarter. On the upcoming products, we have some exciting products lined up for the current and the next quarter like Drop-Line Flexi Loan Product and EMI Cards.

Another significant milestone that we have achieved in the last quarter was that we completed phase-II of our digital transformation. As you must be aware, we had clearly laid down phase II of our digital transformation and we have worked tirelessly towards the same and we now see the deliveries coming in. With the back-end infrastructure ready, and the solution implementation underway, we will see these capabilities getting leveraged now. Phase-II of the transformation has already delivered high impact items of PFL app and WhatsApp journey for the customer service, thus establishing our omni-channel presence. Over the next three to four weeks, we will see the enhanced personalization and customization features go live on the app, along with other enhanced customer journeys. As they say, 'digital transformation is a journey and not a destination'. We remain committed to continuous improvement and innovation, to be quick and adaptive amidst the rapid digital disruptions, enabling us to stay ahead in the game. Despite one-time expenses on the digital transformation, if you see on the OPEX side, there is a decrease on YoY basis.

The numbers on AUM growth, cost of borrowing reduction, drastic asset quality improvement, productivity enhancement, profitability improvement, brand consolidation, digitalization, and technology leveraging, reflects the successful interplay of various elements of our strategy, thereby making this transformation a reality.

I am also happy to note that, as a foundational step, we have embedded the principles of ESG as part of our business process. A board level committee has been set up to provide necessary oversight and guidance.

As we enter the last leg of our Vision 2025, we are well positioned and confident of delivering on the same. It is also time for us to start thinking beyond 2025 and we have already started working on the same. Next twelve months will see us investing in the initiatives, we believe will help us maintain our growth and make us ready for next three to five years and beyond. I firmly believe we have built strong foundation and the next three years should see us fully capitalizing on it.

Now, I will request our Executive Director, Mr. Sunil Samdani, to take you through the Financial and Operational Aspects of the Business. Thank you.

Sunil Samdani: Thank you Abhay and good evening, everyone. Let me take you through the financial and operational updates.

Starting with liabilities, we have seen the hardening of rates over the last two to three quarters. Even then, we've been able to keep our cost of borrowings at almost the same level as previous quarter, currently, at 7.99%. This, we have been able to do through an effective liability management strategy. If you look at our cost of borrowing movement over the last three quarters, the same has come down from 8.04% in Q1 of FY24 to sub-8% in Q2 and Q3 of FY24. This is despite the tight liquidity condition and the higher interest rate in the system. At PFL, since approximately 1/3 of our AUM is eligible for priority sector lending, we will leverage this to minimize the impact of the rising interest rates and we continue to be amongst the lowest cost fund raiser in the industry.

Coming to liquidity, we remain comfortable on the ALM side with positive cumulative mismatch across all buckets and carry a surplus liquidity of ₹ 2,973 crore as of 31st of December 2023. The LCR stood at 127% as on 31st December against the regulatory requirement of 85%.

On the margin side, if we talk about NIM, we continue to maintain the healthy NIM of 11.02% in Q3 of FY24. While on QoQ basis, there has been a contraction in NIM from 11.42% to 11.02%, it is still in line with our stated guidance of more than 10%. This contraction can be attributed to three factors:

1. We continue to focus on the better credit risk segment through credit tested high bureau score customers. To cater to this low-risk segment, the risk-based pricing needs to commensurate with the same, thereby resulting in lower yield and contraction of NIM. As can be seen, there is a reduction in the share of shorter tenure book as the focus is more on income generating assets, and on the consumer side, higher income segment customer. Our play is not driven only by the spreads, but also by the risk adjusted returns which are reflected in our ROA numbers.
2. As we see the rundown in our legacy book and the write-off of our legacy book, which is historically high yielding, we will see the contraction in the overall yields of our portfolio. This will also contribute to the lower NIM. However, it is pertinent to note, as we see the recovery in this return of portfolio, the benefit of that is reflected in the lower credit cost.
3. And lastly, as we make our mix more efficient from the perspective of secured to unsecured, we've increased that from 45% in Q2 of FY24 to 52% secured in Q3 of FY24. We are confident that, while NIMs may contract marginally, with better risk adjusted returns, we will continue to deliver the ROA guidance numbers.

Now, coming to Operating Leverage, we continue to focus on building operating efficiencies across the functions and the same is reflected in our OPEX-to-AUM ratio, which stands at 4% in Q3 of FY24. The same was 4.18% in Q2 and 4.38% in Q1 of FY24. And if we compare it with the previous year same quarter, it stood at 6.06%. This 4% OPEX-to-AUM as on Q3 of FY24, it is pertinent to note that it also includes the ESOP charge, which would be around 0.44%.

Our journey has been exemplary, with increased productivity across the organization. Our ability to scale up business without a linear increase in employee count, powered by high impact technology interventions, has made it possible. The focus on digitization of processes along with use of robotic process automation in operations has helped us make the process faster, error-free, and scalable.

On the customer service side, our relentless focus on providing best-in-class experience has resulted us in offering state-of-the-art customer service through WhatsApp channel. Now, we address more than 70% of our customer service requests through this channel, which is not only digital and instantaneous, but also a self-service channel, thereby making it cost-effective.

Continuing on our DIY philosophy, our app also provides yet another self-service channel to all our customers. WhatsApp as the channel has been a great success for us in customer service and we are now leveraging the same for building an alternate distribution channel in some interesting ways. We have pioneered in providing credit reports to our customers through WhatsApp. We've seen traction there, purely through organic channels and we are also seeing active upsell happening for these customers. This has been a test product for us, and we see this becoming an important part of our distribution strategy. We are also actively using WhatsApp for lead generation, and we will be starting a full loan journey over the next two to three weeks. With this, we will be the first player fully operational on WhatsApp lending, covering engagement through credit report, lead generation, full loan journey and customer service. A complete self-service channel with unparalleled reach ensures that we are present where our customers want us to be. This understanding of customer behavior is a critical element for our distribution strategy.

Talking about collections, we have built a robust collection infrastructure across all our locations over the last couple of years in line with our new portfolio that we have built. We now have a strong hybrid model of collections with a large in-house calling, supervisory and management team of more than 400 employees.

The feet-on-street is well manned with external manpower and multiple partners to ensure no dependencies. The model provides us with complete control on daily rigor being exercised on field through effective review systems controlled via technology. This has helped us to not just being effective, but also remain efficient.

Last but not the least, on the people front we have made steady progress on our people agenda. I'm delighted to share that our efforts to build a healthy workplace with the right culture have started giving results. We participated in Great Place to Work Survey and have been certified as a Great Place to Work. These fuels are for the journey ahead and we make the people-centric future-ready organization.

Thank you, everyone and we can now start the question-and-answer session.

Moderator: We will now begin the question-and-answer session. First question is from the line of Sameer Bhise from JM Financials. Please go ahead.

Sameer Bhise: Thanks for the opportunity and congrats on the strong set of numbers. Just wanted to ask about the growth rates. I mean, we are currently running well above our long-term guidance versus the 35% to 40% AUM growth, we are running upwards of 50%. So, how do you think it over the medium-term and where should we see some bit of moderation and where we should see continued momentum?

Abhay Bhutada: Thank you, Sameer. So our assets under management stood at ₹ 21,946 crore as on 31st December, reflecting growth of almost 58% YoY. The growth has come from the gain in market share of existing products focusing on organic distribution. Over the last two quarters, we have become a significant player in all the products segment that we operate as was stated in Vision 2025. Today, we have a 4-5% market share overall in pre-owned car, business loan as well as in loan against property products on incremental disbursement basis. If we were to look at only top

100 markets where we operate, this is a significant number and aligned to our philosophy of going deep in markets rather than spreading ourselves thin. The focus on the markets and this clinical execution has helped us to grow here. We will strive to maintain and remain in line with our long-term guidance of 35-40% on a yearly basis. Though our base is low but considering the overall thought process of traditional lenders and rating agency in the ecosystem, I think we'll stick to 35-40%. We can grow much higher, but now we will increase our margin. And I think we have predicted this. We need to control the growth. If you listen to Q1 of last financial year, we already predicted that we need to control the growth since the segment which we are targeting is very unique. No one has targeted this segment as we have mentioned in the IR PPT also, that is a combination of bank, NBFC as well as fintech. So, the user experience which we are giving, the kind of rate, fair practice, zero prepayment, I think there is enough opportunity available. Again coming back to your question, we will stick to 35-40% growth and 7-8% QoQ further. We will focus more on increasing profitability, increasing margin, and reducing OPEX.

Sameer Bhise: Also, secondly, on margins, we are tracking above our guidance. Though they have come off on a sequential basis, do you think you will be able to meet the 10% margin guidance despite a 50:50 secured, unsecured mix going ahead?

Abhay Bhutada: Sameer, you're right. Considering secured, unsecured mix, our original guidance was 50:50. Considering that only, since last four quarters, we are giving guidance of 10%, but because of the short-term loans and unsecured loans, we were getting enough margin. So, currently NIM is at 11.03% which is much higher (1% above) than the guidance of 10%. The rationale for the steady state margin of 10% is threefold; the first being, that we focus on a better credit risk segment through credit tested high bureau score customer where the risk-based pricing needs to be commensurate with the same and thereby resulting in lower yield. Our play is not to be driven by spread, but the risk adjusted return, which gets reflected in our ROA number. Secondly, the NIM contraction is because of the rundown of the legacy book and write-off of the legacy book. Because the entire write-off amount is used, especially on the legacy side that gets adjusted in ECL, NCL and that's not getting added into revenue. So, that is the major reason. Actually, in this quarter also, if you see in real sense, sequentially also, there is no reduction in the NIM. But, because of the higher write-off of the legacy book and rundown, that entire amount as per accounting standard, it gets adjusted in ECL, NCL and not gets added to the revenue. Overall if you see the portfolio of that yield was higher because that was agri, CV, tractor, entire cash collection. Lastly, the change in the mix of the portfolio of secured to unsecured, the secured to unsecured from 45% to 55% in Q1FY24, now it is 52% secured and 48% unsecured. So, in the medium term while NIM may contract marginally, but with a better risk adjusted return, I think we will continue to deliver. We are confident of delivering NIM above 10% and again, we are confident on delivering ROA guidance numbers as well.

Moderator: We will have our next question from the line of Kaitav Shah from Anand Rathi. Please go ahead, Sir.

Kaitav Shah: Congratulations on the good set of numbers. I have a couple of questions. Number one was on the app launch. If you can explain two things, what is the current usage and how do you manage credit risk in your app?

Abhay Bhutada: Thank you. We launched app last quarter, and we are seeing good traction on our app. We have been growing on app downloads steadily and now we have downloads of more than 2,000. The rate of increase of download is growing at a rate of 1.5x on a monthly basis. This is while we are promoting the app organically and not doing any burn to drive the download. We see a very healthy daily active user metrics of about, let us say, 13% to 14%, which is one of the best for any lender. Also, our uninstallation rate is less than 15%. We are continuously refining our app journey and adding more and more features to drive the engagement. The typical maturity, if you see curve for any app is anywhere between 9 to 12 months and we see our app is on the right track. Risk management in app lending is based on the right customer selection. We follow a consent-based architecture and leverage consented device data through the app for better customer understanding. We use our proprietary scorecard; we are providing risk-based pricing and multiple loan offer to the customer. We ensure that identity checks including KYC are done online and we insist on Aadhaar checks also. As a risk strategy, we only focus on credit tested customers and with a bureau score of 700 and above for entire personal loan and other loan products as well.

Kaitav Shah: Sir, can you talk more about the co-branding with IndusInd and how that's likely to pan out over the next six months, is it like in place or not in place?

Abhay Bhutada: Last quarter, we received this co-branded card approval. Now, integration is under process. A few things are pending with co-branded card which is at IndusInd Bank’s end in terms of IT integration and a few other things. I think we will be able to launch this in the month of March. And this will be a complementary product to our existing product basket, because this will help us to engage with the customer in the day-to-day transaction and overall with the increased penetration of this digital payment co-branded card, it will again help us become an active participant in the payment ecosystem. So, we see a sizable opportunity here in the segment in which we operate. Here also, we will target only the pre-approved set of customers and we can do a lot of cross selling here once we launch this. We will launch in March month. We don't want to be in a hurry because the segment again, in which we are launching, the joining fee will be zero, the annual fee will be zero, there will be two variants to start with. So, it is a unique proposition. Whatever we did in the past, if you see any of the products, we are not launching anything which is available in the market. If you compare it with any other NBFC co-brand card, this will be much more beneficial if you talk about the customer-centric approach.

Kaitav Shah: In terms of understanding, what is the organic percentage for acquisition, I mean, in your disbursements how much is acquired organically today and what is the target there? I got the secured and unsecured bit. Given that all your other channels have started firing or are about to launch, what is it that you see over a two-year period?

Abhay Bhutada: Correct. Over a two-year period 100% will be organic. That was our strategy initially to do the co-lending and then we stopped onboarding the new customers from September onwards via co-lending. Now, in digital we have done almost ₹ 3,600 crore on the cross sell, on the direct side, we did almost ₹470 crore, DSA was almost ₹ 1,733 crore, then the remaining partnerships, so, total almost we did ₹8,731 crore. Right now, if you see, overall organic is almost 80%-plus. And with the guidance of 35-40% AUM growth instead of 58%, 60%, two years down the line it will be 100% organic. But initially, we tested the customer, and we onboarded the customer and we gave them short term to medium term and long-term loan, and we have started cross selling. So, now everything is in place. We have gone digital across all the products. We never thought we would be able to reach 80%-plus at such a short span of time.

Kaitav Shah: With your secured book at 60% and with our scaling now in size, does the model of sourcing you think still remain the same mode of fintech or we'll see more branches coming to play?

Abhay Bhutada: We focus on top 100 markets, and we are increasing our market share in these markets, and the guidance is only 35-40% considering the low base. We believe that overall there is enough headroom to grow there. The segment which we are targeting, as I said, they are getting user experience, they are getting practical approach and cash flow-based lending approach like NBFC and fair practice, zero prepayment and rates like a bank. So, mix of secured to unsecured is not changing drastically to call for any physical distribution change. Even on the PoC side, LAP side, we have started call center and are digitally including cross selling. We are targeting entire products digitally. So, we don't require any additional branches, unless we cross ₹50,000 crore loan book and the current manpower also, if you see, we are one of the best in the industry in terms of productivity. We have crossed almost ₹10 crore AUM per employee, and with this current employee base, and with the current branch infrastructure, I think till ₹50,000 crore we don't see any challenge. And as and when required, we can always grow the branches, we can grow the manpower step-by-step, but I don't think so for next two, three years there is any need.

Kaitav Shah: If you can talk about the competitive intensity right now in the consumption lending space, how is that looking post the risk weight changes?

Abhay Bhutada: I think this is much more beneficial to Poonawalla. If you see our leverage is 1.5 and the capital adequacy is 38%. A very few players are offering. If you see the slide #9, we have actually demonstrated this very well in terms of each of the parameters in terms of loan amount flexibility, collateral-free loan, quick turnaround time, 100% digital process, low hidden charges, low interest rate, zero prepayment charges, flexible tenure, and minimum document. So, it is a combination of so many parameters. This is what I call as the ethical lending with a unique product proportioning and customer-centric approach. So, I think there is a huge opportunity for a player like us who has capital risk management practice and entire digital is in place, I don't see any challenge. We discussed it multiple times in the investor call in the past also. We are not in a competition with any of the NBFCs. As of now, we are competing with only top three private banks. Because in terms of distribution, technology and in all the other parameters, now I think we are at par with either top three banks or top three NBFCs. But, in terms of fair practice, in terms of rate of interest, in terms of unique product propositioning, I think there is no competition, because it will take time to copy this business model, it requires ethical lending mindset to target these kind of segments and we further get right to select in this kind of a market. In terms of capital challenges, it is an opportunity for us. A lot of other NBFCs with a leverage of above four, they're reducing their unsecured loan. And despite the sale of housing, we are able to maintain 50:50 secured and unsecured. So I think whatever circular we have got from the RBI, we will welcome all the suggestions and whatever tightening norms are there. I think last quarter also somebody asked a similar question much, much before this RBI circular and we said the same thing. I think Poonawalla Fincorp will be more beneficial as compared with any other player in the market for any tightening of the norm, because from day one, I think, we are completely aligned on all these circulars, and we are following most of the norms like a bank. So, there is no impact of any of these circulars till date on the Poonawalla Fincorp.

Moderator: We will have our next question from the line of Renish from ICICI. Please go ahead.

Renish: Sir, congratulations on the good set of numbers, just two questions. Once, again, sorry to circle back to the RBI circular. But if you look at the commentary, whether it is on the risk weight side, the NBFC lending or banks or whether it is a commentary on the unsecured loan growth side, is there any implication on Poonawalla, either in terms of higher cost of borrowing or moderation in growth?

Abhay Bhutada: Just now few points I've explained to Kaitav also. RBI has shown concern around unsecured lending for consumption purposes and specifically in certain ticket sizes. See, the regulator wants this to be rationale and put-up practices to be followed. In this backdrop, the risk weight on this asset classes were increased and there has been tightening of credit to institutions solely focusing on the segment. We have a very well diversified product base, and we don't have any large concentration. We hardly have any leverage and with debt-equity of 1.5%, capital adequacy of 38% against the regulated requirement of 15%. We have a healthy portfolio mix where secured constitutes 52% and unsecured constitutes 48% and we will be able to maintain 50:50 as per our guidance. On unsecured side, we have a good balance of MSME. Unsecured does not mean forming the largest component of our book. The impact on our capital adequacy of the higher risk weight was 220 bps for us and we are sufficiently capitalized. So, as we move ahead, we will continue to grow across segments while exercising due caution. And we don't see any cost of borrowing impact also, reason being, we are CRISIL AAA rated, and leverage is 1.5, lowest in the NBFC segment. So if you see in QoQ basis also, hardly there is a 1 bps impact. Still, there is a legacy borrowing left of around ₹300-400 crore which is at a much higher rate. Technically speaking there is almost a decrease in the borrowing cost, or it remains flat. So, we don't see any challenge there as well.

Renish: Secondly, I'm referring to slide #15 of the PPT. When we have disclosed the legacy book data as on December '20, can you just throw some light like say as on December '23, how much of the legacy book is still there on the balance sheet? And in terms of the 1.3, 1.4% gross NPA, how much of that is still coming from the legacy book?

Abhay Bhutada: Basically, if you see the legacy book now, we have mentioned the AUM breakup also. From the AUM side, now, only DA and the legacy book is left. See, in slide #24, discontinued legacy plus DA is ₹ 1,822 crore which is 8% of the total book. Out of that, DA was acquired book and legacy now is less than ₹ 200 crore. Maximum we have, either written off or we have provided. That is one. Secondly, if you see the net NPA of the new book is just 0.23% and the remaining NPA of the legacy discontinued book is 4.88%. So, on the co-lending partnership side, the GNPA 90-plus is 1.76%, net NPA is 0.93%. However, we are not incurring any losses here because it is backed by FLDG. In case of new origination, the GNPA is 0.42% and net NPA is 0.23%. The new book is performing well. We have almost completed three years post-acquisition. Then, if you talk about the discontinued plus this legacy and acquired book, their GS3 is 9.04% and net NPA is 4.88%. That's why because of this 9% of GS3 net NPA of 4.88%, you see the total comes to GS3 1.33% GNPA and net NPA to 0.70%. Otherwise, let us talk about new book which we originated, it is 0.42% and 0.23% against our given credit cost guidance of anything between 0.8% to 1.2%. Because of our strong risk culture in the organization, the new book is performing better than our expectation.

Renish: While you touch upon the operating leverage part, but if you can just explain us this 4% cost to aside settling it or let's say in the next couple of years?

Abhay Bhutada: Currently it is around 4% in Q3FY24, which was 4.18% in the last quarter and 4.38% in Q1 of FY24. If you see the similar period Q3FY23, it was almost 6.06%. This 4% also includes the ESOP cost of almost ₹ 22 crore. Basically if you see, 0.45% is the ESOP cost. So, already we are at 3.5% without ESOP. Considering this next financial year, you can expect on a yearly basis, OPEX-to-AUM, it will be less than 3.5%. And this is despite of one-time cost, so many consolidation costs, a lot of digital and the IT cost. So, I think we have achieved better than our expectations.

Moderator: We will have our next question from the line of Sameer Bhise. Please go ahead, sir.

Sameer Bhise: Just two quick questions. We have seen strengthening of the board with new induction. Do you think there are any more changes possible from an executive side? And secondly, can you comment on the credit cost outlook?

Abhay Bhutada: So, on the management side, last quarter, we inducted Executive Director, Mr. Sunil Samdani. And since we are growing, it is an ongoing process, we will recruit additional senior people as and when required, and we will strengthen our board who will help us sail through our next phase of growth. On the credit cost side, we have always guided anything between 0.8% to 1.2% on a steady state basis.

Moderator: We will have our next question from the line of Mayuresh Joshi from William O'Neil. Please go ahead, sir.

Mayuresh Joshi: My first question was that as you put on in slide #27, and as you mentioned in your commentary, you become a meaningful player in the pre-owned car market. So, how do you see this part of the business growing further? And other products, specifically the digital-led product innovation that you're pointing to, how is that looking, sir?

Abhay Bhutada: Overall growth for us has come significantly from the gain in market share of the existing products. But, over the last two quarters, we have become a significant player in the product segment that we operate. For example, in pre-owned market also, now share is almost 5% on an incremental disbursement basis. With the same share, we are in business loan and loan against property. We have crossed ₹225 crore in pre-owned car on a monthly basis. In business loan, we have crossed more than ₹250 crore on a monthly basis. Loan against property, we have crossed ₹350 crore. Loan against property, we operate only at 40 branches. Business loan around out of 60-70 branches and pre-owned car is also around 60-70 branches. So, there is still enough room available. Road map clear cut. We can see we will take a major market share in the top-100 branches and that's why we are confident that the segment which we are operating in, there is a huge demand and within 100 branches itself we will try to increase major market share across these three - four products, and again on the consumer side also, now we have completed the digital transformation. You will see in the next two years the huge transformation on the consumer finance side also because we will increase the market share there as well.

Mayuresh Joshi: Just adding on to the point on the transformation bit that you just put forth, the transformation in the past two years has been absolutely superb, nothing short of a miracle. Can you just explain investors in brief, I mean, I would just like to understand how did you do such a quick turnaround for such a good amount of transformation that happened?

Abhay Bhutada: I think I will say the strategy. Poonawalla Finance was unlisted NBFC of the group. So, we have learnt most of the things there in Poonawalla Finance all the unsecured product, personal loan, professional loan, and business loan, and post-COVID we have come out with a different skill set altogether. We recruited if you see our all-senior team, those who are with us, they all come from Poonawalla Finance. Therein, the equity was more than ₹ 900 crore and we wanted to scale up at a pan-India level. And then we got this Magma opportunity, and then because of the collection in front, and so many other reasons, we acquired this. Considering that, if you see, we have very strong strategies in place, again unique proposition which is a combination of, we always say, fintech backed NBFC. And because of this, unique business model, technology, system, process, risk management, risk culture, people, the speed of execution, the innovation, and the vision of the management. There are so many reasons, I think we have never expected, even at our level, that we will be able to transform so quickly. Now, 80% of our total time we have given to resolve the existing consolidation, legacy issues, legacy manpower, because we acquired that entity, which was into cash collection, CV, tractor. Now we have completely transformed, and I think we're absolutely on track and you will see fantastic growth, superior profitability and good asset quality going further.

Mayuresh Joshi: On the digital-first initiative that Poonawalla has incorporated over the last few quarters, the transformation on the digital front is yielding results. Would you like to through some color in terms of the robotic interfaces, the HTTPs, and the multiple self-service channels because I think this is one example that you gave, where Poonawalla probably stands out compared to the rest of the NBFCs pack?

Abhay Bhutada: Basically, if you see on all the parameters, it is a differentiated business model and a branch-light model as well as non-conventional. So, we have well defined all the risk policies, digital-led and branch-led model that differentiates from all the conventional models. And again this model is resulting into lower operating expenses, at the same time it is enhancing our operational efficiency also. We have invested hugely on the web platform, on the app platform, WhatsApp platform. These are all giving results. On the technology and innovation side, I think from day one we have gone digital across all products on the e-sign, eNACH, eKYC, e-disbursement, e-collection. We have been using BRE since day one, we are using algorithm-based lending risk-based pricing, we are using data analytics, one of the best in the industry supported by AI and ML and again unique product proposition also. So, these are helping us. If you see, again, it requires mindset. All FinTechs are giving superior technology but are they able to provide the better rate to the customer or are they able to leverage balance sheet properly, are they getting lower cost of funds? Other than technology, we are getting this lower OPEX and the lower cost of fund which is resulting into the segment targeting with lower credit cost and that is the result of one of the best Return on Assets in the industry.

Moderator: Ladies and gentlemen, that was the last question for today. I would now like to hand over the conference to Mr. Hiren Shah for closing comments. Over to you, sir.

Hiren Shah: Thank you, everyone for joining this earnings call with us. For any further queries or communication, please write to us at investor.relations@poonawallafincorp.com.

Moderator: On behalf of Poonawalla Fincorp, that concludes this conference. Thank you for joining us and you may now disconnect your lines.