"U GRO Capital Limited Q3 FY20 Earnings Conference Call"

February 3, 2020

MANAGEMENT:	**MR. SHACHINDRA NATH – EXECUTIVE CHAIRMAN & MD** **MR. ABHIJIT GHOSH – CEO & WHOLE-TIME DIRECTOR** **MR. KALPESH OJHA – CFO** **MR. VIVEK SESHADRI – HEAD OF STRATEGY & INVESTOR RELATIONS**
MODERATORS:	**MR. SHREEPAL DOSHI – EQUIRUS SECURITIES PRIVATE LIMITED**

Moderator: Ladies and gentlemen, good day and welcome to the U GRO Capital Limited Q3 FY20 earnings conference call hosted by Equirus Securities Private Limited.

As a reminder, all participants' 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 '*' then '0' on your touch-phone phone. Please note that this conference is being recorded.

Before we begin, I would like to mention a short cautionary statement. Some of the statements made in today's conference call may be forward-looking in nature. Such forward-looking statements are subject to risks and uncertainties which could cause actual results to differ from those anticipated. Such statements are based on management's beliefs as well as assumptions made by the information currently available to the management. Audiences are cautioned not to place undue reliance on these forward-looking statements in making any investment decisions. The purpose of today's earnings conference call is purely to educate and bring awareness about the company's fundamental business and financial quarter under review.

I now hand the conference over to Mr. Shreepal Doshi from Equirus Securities Private Limited. Thank you and over to you, sir.

Shreepal Doshi: Good evening everyone and a warm welcome to you all. We thank the management of U GRO Capital for allowing us to host their 3Q FY20 results update call. On behalf of the company and Equirus Securities, I would like to thank you all for participating in the company's earnings conference call. On the call from management, we have Mr. Shachindra Nath – Executive Chairman & MD, Mr. Abhijit Ghosh – CEO & Director, Mr. Kalpesh Ojha – CFO, and Mr. Vivek Seshadri – Head of Strategy & Investor Relations.

We will start with the opening remarks from the management followed by Q&A. Over to you, sir.

Shachindra Nath: Let me start with my opening comments. The challenging macroeconomic condition for the lending sector, particularly the NBFCs, has persisted in quarter-3 FY20. With uncertainty regarding resolutions on IL&FS, DHFL, Reliance, and Altico as well as the continued lack of sufficient liquidity. This has been exacerbated in the SME space by elevated NPA level making borrowing yet more expensive. However, we are pleased to note that U GRO continues to navigate these rocky waters well thanks largely to our conservative credit approach at this time. We will try to maintain our steady and controlled growth going forward, scaling at an excellent pace while concurrently ensuring that our loan portfolio is pristine.

Our aspiration is to build a highly technology-driven small business financing platform with a portfolio construct which is reflective of a traditional NBFC. We are gradually moving towards high degree of digitalization in our business, and over a period of time, our technological prowess with our conservative portfolio approach should not only give us the scale and operating leverage but also create a highly robust portfolio.

Moving onto the quarter, this quarter saw us reach 1073 crores of total disbursal and inclusive assets under management of 753 crores, which are excellent figures to have achieved only in 1 year of lending operations, let alone in the current market conditions. This quarter saw the launch of our direct digital channel GRO-Direct which we anticipate will become a revolutionary method of providing eligible customers with a non-intermediated access to financing. The beta launch of GRO-Direct in December was limited to only two of our sub-sectors and yet we have already achieved our first disbursals through this channel.

Quarter-3 has seen us to take great strides towards achieving the full potential of our 4-pronged distribution model. Not only have we commenced our final remaining channel in digital lending, we have also disbursed our first loan against machinery. These are portents of our vision to provide a broader set of products with the highest level of specificity possible to Indian SMEs. We continue to disburse at a similar rate to quarter-2, with a slight drop in disbursal numbers from 402 crores to 372 crores that is accounted for by our desire for conservative portfolio construction, particularly for the first 1000 crores of our assets under management. Our AUM growth has progressed well and now stands at 753 crores, up from 575 crores at the end of the last quarter. It is spread across 7512 loans for a highly granular average loan size of Rs. 10.6 lakhs.

Our traditional channel continues to perform efficiently. We have increased our GRO partner network by 34% quarter-on-quarter to a total of 311 spread across key SME clusters in India. Our GRO-Plus app is undergoing continual improvement, and this is being reflected in superior turnaround times.

Our ecosystem channel saw growth in this quarter with 5 incremental anchors added bringing the total to 21. As a result, we have been able to onboard 62 more vendors and increase our supply chain finance assets under management by 41 crores. We have also started building partnerships to disburse loans against machinery with a partnership already signed with Ace Micromatic Group. Development is ongoing for GRO-Chain which will be an all-encompassing platform to facilitate end-to-end supply chain financing when launched.

The BFSI channel has seen significant successes with our first secured co-lending loan disbursed in November through our partnership with CIHL. We have now disbursed both secured and unsecured loans through our co-lending partnerships, setting the table for tremendous growth opportunities in future. We are also very proud to have announced a co-origination partnership on the liability side with ICICI Bank, the largest private sector bank in India. ICICI Bank joins both State Bank of India and Bank of Baroda as premier financial institutions who have placed their trust in our ability to source and underwrite high-quality books.

The biggest development for us this quarter was of course the beta launch of our direct digital channel GRO-Direct. This is a project we have been working on for a long time and this quarter saw the completion of both our web-based and chatbot-based journeys, the former of which is now live while the latter is awaiting API integration. While we are undoubtedly delighted with the successful release of GRO-Direct, we have ambitious plans for this channel which we believe can revolutionize the SME lending space and we can't wait to share our progress on this front with you going forward.

Our overall portfolio is well diversified by geography and sector and two-thirds of our book is secured, all of which are how we would like them to be. The performance of our portfolio is excellent and our GNPA stands at less than 0.1% despite our book now showing some vintage.

On the liability front, we have raised a total of 194 crores from 7 institutions including Kotak Mahindra Bank. This number has been modulated by an amount of cash we have had on hand and we expect to be able to significantly grow this number in the quarters ahead.

Our capital structure underwent some changes as Samena Capital, one of our shareholders, exercised 66.2 crores worth of warrants this quarter, which we saw as a capital infusion. With this, there are no longer any further dilutive instruments outstanding.

U GRO's financial performance saw a monumental shift as we have achieved profitability within 1 year of commencing lending operations. The company's net worth now stands at 901 crores and our net income has increased by 15.4% quarter-on-quarter to 23.7 crores. Our quarter-3 PBT stood at 5.8 crores driven by a combination of rise in revenue and fall in cost. We remain highly liquid, which we consider a necessity in these times of constrained and expensive liquidity. Overall, we are happy with the direction of the company as we feel we are taking the right steps, and this is getting reflected in our performance over time. We hope that you will keep faith with us and afford us to demonstrate the culmination of our collective aspirations. Thank you all. Over to you Shreepal and the Equirus team.

Moderator: We will now begin the question & answer session. Ladies and gentlemen, we will wait for a moment while the question queue assembles.

The first question is from the line of Anadi Kaistha from Vivriti Capital. Please go ahead.

Anadi Kaistha: Congratulations to the U GRO team for the good set of numbers in this quarter. Sir, there are a couple of questions which I want to ask. First is regarding the average ticket size. If I see the average ticket size, it has increased for both the secured and unsecured segments. What is the reason for that? Because in the current scenario, everybody is going for a smaller ticket size. Can you please throw some light on that?

Shachindra Nath: If I understand it correctly, you are saying our average ticket size from last quarter has increased. Is that what your question is?

Anadi Kaistha: Yes sir.

Shachindra Nath: I don't think that will be the case. Vivek, can you confirm?

Vivek Seshadri: Yes, it changed slightly to the north. It has nothing to do with our difference in strategy, etc. It's just to do with the originations. Obviously, quarter-on-quarter, those numbers, the origination mix – the channel mix – changes a lot. This time the emphasis was more around the traditional branch-led channel and the ecosystem-led channel vis-a-vis the partnership-led channel and that's the reason why you have seen an increase in ticket size.

Anadi Kaistha: But, I have seen that ticket size has come down for all the companies in the same sector, for secured and unsecured. So, this was a little surprising and again, the average yield is also coming down. Like in Q2, the average yield was 12.7%. Now, in this, the average yield is 11.9 for secured loans. In case of unsecured, against 18.8%, it is 18.3%. So, is there any kind of cost borrowing benefit which is being passed on to the clients or so?

Shachindra Nath: Let me give you a broader strategy and that will give you some sense of how our portfolio gets constructed. As we explained that U GRO has a 4-channel strategy, we have a channel which we call intermediated or our traditional direct channel which is driven by our platform called GRO-Plus. Then, the second channel is our ecosystem channel which is supply chain financing. Third is our BFSI channel wherein we co-lend with the smaller NBFCs. We are also looking at their portfolio and providing liquidity through that. And fourth is our digital channel which has not started yet. So, the average ticket size is a function of, in a quarter, which channel has done well. Our core intermediated or traditional channel deals in secured ticket sizes of anything between starting from 50 lakh to 5 crores, and our BFSI co-lending channel provides a much more granular portfolio. In the last quarter, we had a defined strategy to build our direct channel sourcing much bigger than our indirect channel sourcing and that's why there is an incremental ticket size upgrade. It means, these average portfolio ticket sizes would keep changing depending upon which channel we have utilized for onboarding the customer base.

Anadi Kaistha: My second question is with respect to the employee expenses. The employee expenses are highly fluctuating. Though it is growing, and we are hiring new employees also, but still like if I see so, in Q1, it was 11.2 crores; in Q2, 14; in Q3, it is 10. Is there any specific reason for declining employee cost in Q3?

Shachindra Nath: Last year was our build-out year, so as the current year itself. And in our build-out year, there are certain costs with respect to employees for which we do provisioning and then we change those provisioning norms depending upon what we see would come as an actual expense. The thing is that we are at the end of the last quarter of the financial year, some of the provisions which we have done towards benefit of employee pool, we thought that that would not actualize and that's why, those provisions have reversed and that's why you see a fluctuation in the employee cost. And what you are seeing at least for the next 2 quarters is our run rate cost.

Anadi Kaistha: Sir, with respect to operating expense which is mentioned in the debt that there was some specific course due to which operating cost was high in Q2. Can I get some sense of what kind of operating expense was that?

Vivek Seshadri: Last time around in relation to the set up of the company, we continue to incur certain legal costs and certain hiring related costs as well. Those are all one-time costs which are related to foundation. For instance, we needed to draft multiple customer agreements, there were certain new employees hired because of which there was a fee paid to headhunter, so on and so forth. Those costs have gone down to zero in this quarter and this is going to be the steady-state expense level going forward if you will.

In the last presentation, these expenses were specifically called out.

Anadi Kaistha: Sir, my last question is with respect to the concentration of clients. What would roughly be the concentration of top 50 clients in the total AUM?

Vivek Seshadri: We will get back to you with those numbers offline. We don't have those numbers handy with us right now, but that is not going to be a very high number. It will be less than 15% of the book.

Shachindra Nath: Just to broadly answer, our sectoral distribution of our portfolio is very diverse, the highest being roughly around 18% which is food processing and then going downwards. Secured is 67% and unsecured is 33%. Geographical dispersion is also very broad, highest being 30% in Gujarat and lowest being 1% in NE states. From both sectors as well as geographical dispersion, we are very granular.

Moderator: The next question is from the line of Kaitav Shah from Anand Rathi Financial Services. Please go ahead.

Kaitav Shah: Congratulations on your good set of numbers. Sir, I just wanted to check with you on the cost of funds trajectory for you. How is it for December quarter and is it different in January or going forward?

Shachindra Nath: We have just started our liability program. As we know, till last quarter, we have been funding our book largely through equity. We started our liability program a little earlier than we exhausted our equity because we maintain an X amount of cash and we intend to do that going forward as well. And that's why this leverage has come in. As we have mentioned in our debt that our blended average cost of liability today stands at 11.5%. It is very difficult to predict what would be the cost of liability going forward. Obviously, the endeavor is to bring it down further given the size of equity capital and the kind of granular and secured portfolio which we are building up, but simultaneously also we have deep focus on building our co-lending partnership and operationalize them because while they are not on balance sheet liabilities but they are great source of earning for us.

We are working very hard to operationalize our partnership with Bank of Baroda, SBI, ICICI, and there are a few more partnerships which are in the line. And we hope that few of them would become fully operational wherein we will start disbursing loans on the co-lending basis and obviously the revenue portion of that is very attractive vis-a-vis on balance sheet borrowing.

Kaitav Shah: And can you explain where this co-origination model has reached in terms of the entire piece?

Shachindra Nath: Yes, of course. I would specifically like to answer that because I think there is a general skepticism within the analyst fraternity that co-lending model has not worked for the industry as a whole. We generally believe that going forward for NBFCs, on balance sheet borrowing vis-a-vis some form of off balance sheet businesses would take precedence. That can be in the form of co-lending securitization or multiple types of similar structure and also we believe that the matured players who have the capacity to borrow on balance sheet are gravitated more towards lendings on their own balance sheet versus working very hard to build any co-lending model.

We have a few very major headwinds and against that, we were successful in signing up 3 partnerships. First, that we were competing against some very established players in the market wherein most of these large financial institutions like to have vintage, both entity vintage as well as portfolio vintage and some threshold rating parameter. We crossed the hurdles of rating parameter but we didn't have entity vintage and portfolio vintage, but eventually most of the large lenders saw the power of our statistical underwriting and the granular underwriting approach and our sectoral specialization which we bring on the table, and that led to, after a hard effort, signing with three of the large lenders. That's point number one.

Number two, in terms of operationalizing, as we said, we had signed up with all three of them. We are in the process of putting the operating matrix and finally the legal mechanics, and last but not the least, putting the technology behind it.

You need a very defined approach in terms of how you will operate on granular small loans in terms of your co-lending, and we launched our platform which is called GRO-Xstream which has this ability to retune our own policy and align that with a large bank, and a system automatically picks up a loan file and takes it to the banks where it is more suited.

All of that being done, that's why I said at the beginning that we are hopeful that in the next quarter, we will see some disbursement happening on a co-lending basis with at least two of the three partners we have signed up.

Kaitav Shah: And in terms of the overall asset quality outlook going forward as well, given that there is some pain visible in MSME, banks are slowing down. What are you hearing from your employee base about stress in the MSME sector?

Shachindra Nath: Obviously, the first and foremost, we are not denying the fact that generally the small businesses and micro businesses are under stress. They are under stress on two fronts. This stress started from demonetization, made worse by GST, and then became accentuated with the liquidity crisis, and then also growth trajectory reversing towards a lower growth. And all coupled with that have put the small businesses and micro businesses' cash flow under severe stress. Having said that, our belief, without this the current market, has always been that there is a correlation between the gross yield of the loan to a loss ratio. And we think that the majority of the stress currently is in the micro SME segment at the highest strata of the loan yield. So, NBFCs or businesses which are in that 25% to 30% and 35% yield segment you will see an expanded loss ratio. From an average of 3%, it should now go to 6% to 7% but the prime market which is the small businesses secured between 11.5% to 12.5%, you will see that pain to be lesser. Our founding strategy has always been that as a new entrant into the market, we would first build our portfolio in the prime segment and not go to the micro segment directly on our own. Wherever we are doing micro segment, that we are doing on a co-lending basis wherein we have some form of a first-loss cover and an underwriting or a geographical spread which is controlled by a partner NBFC of ours. And we have tightened our underwriting norms further. So, our underwriting is driven by the statistical bureau based altered underwriting where we have moved our cut off to even further upward trajectory even if it comes at a sacrifice of a little bit of yield.

So, I think that broadly the NBFCs would continue to suffer with increased gross NPA ratio, especially players who are playing the MSME market or even a shade below that. But for us, we think that this is the right time to build a quality portfolio because there will be a lot of players who will be exiting because of these challenges.

Moderator: The next question is from the line of Sumit Bhalotia from MK Ventures. Please go ahead.

Sumit Bhalotia: Congratulations for the good set of numbers. Blended cost that you have mentioned is around 11.5, right? That would include some of the borrowings that would have been done against the cash that you are holding. Is that true?

Shachindra Nath: No, that's not true.

Sumit Bhalotia: So, we can still borrow at 11.5% in the market?

Shachindra Nath: The cost of liability is on our balance sheet. It is not backed by cash or cash-equivalent collateral. In fact, we carry cash on a negative spread because we have borrowed some money and kept it in FD. So, we expect our future cost of borrowing to be in the same range or come down because our public sector borrowing has yet not started, not because banks have not approved the credit but it is just slower for us because as you know that U GRO's board is majority of independent directors. It has been provided in our articles that we will always maintain a board which is majority independent directors. Out of our 7 independent directors, there are 4 directors who are on the board of the other banks, and as per RBI's circular, it necessitates that every bank who we apply for a loan to has to take our proposal straight to their board of directors. That just elongates the process of our sanction but now we are at the end of wherein at most of the banks it has already reached at the top and we should start seeing the incremental borrowing to come from diversified set of lenders right from small finance banks, private sector banks, and public sector banks. Hopefully, that should bring down our incremental cost of borrowing a little bit from where we are today.

Sumit Bhalotia: Obviously, we will be completing 1 year of full operation. That would also give comfort to a lot of banks in terms of term loans, right?

Shachindra Nath: Absolutely.

Sumit Bhalotia: I understand this co-lending model is progressing well for us but it is just taking time to get converted on a monthly basis, the actual borrowing to start. Assuming that you start operations with all 3 banks that you mentioned – ICICI, Bank of Baroda, and SBI – what is the monthly quantum or a quarterly quantum of funding that you are looking at say by next 6 months? And how would your overall spreads and NIMs change once you are able to achieve that?

Shachindra Nath: I think that this is too new for the market, Sumit. So, the way we are approaching that we are creating capacity in our origination engine, which is roughly around now 100 crores a month. We should be able to fulfill the need of that through on balance sheet borrowings, but we are very clear that as soon as these partnerships get operationalized, we would start flowing these assets through these banks. And most of these partnerships are in the range of 20-80 or 30-70 splits, but it is very hard for me to predict whether we will achieve disbursement through co-lending in the next quarter itself. I am hopeful of getting at least as I said, two out of these three operationalized and I think by the 1st quarter of next year, we should get full scale on that. But as of today, we are not dependent upon these co-lending partnerships to start operationalizing at a full flow and that's why we intend to continue building our on balance sheet borrowing capacity including doing securitization. As of yesterday, we did our 2nd securitization transaction as well. In the early stage of our operations, we have already done 2 securitization transactions. So, we are building a track record of all sources of liquidity and financing for ourselves and we are quite successful in doing that in spite of the very difficult market circumstances for all the NBFCs.

Sumit Bhalotia: Do you have any target securitization number in mind? I am trying to understand the funding part of the book. Also, we are going fairly quickly now. I think we are on track to achieve more than around 1100 to 1200 crores by year end going by the run rate that we are doing. I am just trying to understand that by FY21 end, whatever AUM we have, how are we going to fund it because our equity is now exhausted mostly and we would be keeping some cash buffers at least for the next few quarters. If you can give some color on that what percentage of portfolio would be securitized?

Shachindra Nath: I get what you are trying to ask. And I am finding it a little difficult to predict that. We are very confident that the year 2021 number even if these co-lending partnerships would have not been there, we would have still been able to maintain our run rate and we have no doubt about it. But our aspiration or expectation is, a large portion – at least 50% – of that to come through co-lending because our spread on co-lending is superior to our on balance sheet borrowing.

Vivek Seshadri: And just to add to that point, it is not as if traditional liability is not available. We already have 240 crores of, as we speak, debt on our balance sheet today. And that essentially is lying as cash on our balance sheet as well. So, it is not as if traditional debt is not available. But obviously efforts are underway to increase the co-lending output as well. And I think you should have very good clarity on this when we talk in the next call.

Sumit Bhalotia: Last question on the target ROA and leverage for say FY21, if you can give some range for us?

Shachindra Nath: We are too young for that, Sumit, because our personal view is that we should demonstrate asset growth. We should demonstrate reduced cost of borrowing. We should demonstrate our technology capability which is now coming up very well and that's why if you see yesterday's press release, we compared ourselves to fintechs for the first time. There are many fintechs who made lot of noises but burned so much of cash while we are actually equal to any fintech now. We can say with confidence that in terms of our technology prowess, we are equal to any of the fintechs in the country but we have turned profitable. But what would be exact return on asset I think is a little early. Give us 2 more quarters and I think that we should be able to get a better indication. It is also a function of, as I said, depending upon how much of on balance sheet and off balance sheet we will do and depending upon that, our return metrics would set in.

So, I think that at this point in time, we would like the investor and analyst fraternity to track us on our growth rate and other parameters and have confidence that in a few years, we will scale this business and achieve superior return on equity and return on assets compared to, I am not talking consumer finance businesses, but for small businesses' finances, we should be better than most of the peer set predominantly because the way we have designed our distribution and our off balance sheet capability now.

Moderator: The next question is from the line of Rahul Singhania. He is an individual investor. Please go ahead.

Rahul Singhania: Congratulations on the good set of numbers. Sir, my question is on the lending which we have lately started against the machinery. What is basically the loan-to-value ratio we try to maintain over there as compared to the other segments that we have? And if you can also give me some information on the lending rate what we have there?

Shachindra Nath: I would request Abhijit to give you the answer for the specific issue you have asked. But let me give you a color in terms of what does it mean by loan to machinery. As you know that we have designed this business to finance 8 specific sectors in the market and then 38 sub-sectors. And we started with what we call our portfolio with a collateral of mortgages which is residential mortgages and commercial properties and some industrial properties. But we believe that that is not productive financing. Ultimately, the productive financing is that when you are financing the asset which is being created by the small businesses.

In our healthcare, dental clinics is a sub-segment which we operate, and we have to start thinking of can we finance the dental chair. The way we approach is that we have now a partnership with a manufacturer of a dental chair who has given us comfort that he understands what is the residual value of the dentist chair. He gives us the comfort that for some reason if the doctor defaults, then he would be able to bring that dentist chair, refurbish it, and sell it to somebody else. So, we don't want to do machinery or what we call productive asset financing unless and until we have an ecosystem partnership in terms of the realizable value of that asset and we understand that sub-segment very well. So, our approach is that for every sub-segment, once we have reached to a little scale, we understand that sub-segment very well, then we start doing the productive financing. That's broadly the strategy. In terms of loan to value and the gross yields, Abhijit, you want to comment on that?

Abhijit Ghosh: First of all, as Shachin said that we will be looking at various machineries. We just started it last quarter. Now, we are doing the bottom of it which is lathe machines, CNC machines, and stuff like that. We do tie-up with the manufacturers; Ace being one of them, BFW being one of them, Jyoti being one of them; these are the ones that we have tied up. In this, we have started but as we go forward, our aspiration is to move towards dental chair equivalents as well but that will happen over a period of time, maybe a few years. But we will go towards those kinds of machinery as well. Having said that, these are standard assets and we operate at an LTV of anywhere between 60% to 70% with a manufacturer assurance that tomorrow in case of a challenge, we will jointly work out the redeployment of the asset.

Rahul Singhania: The dentist example which you gave of having 38 sub-sectors, this was basically an example of ecosystem lending model, right?

Abhijit Ghosh: Correct.

Rahul Singhania: Can you try to name some partners what we have, sir, in this ecosystem model? And also if you can throw some light on what kind of the model is over here? Basically how much cost is it for us and all, the further to that?

Shachindra Nath: I think that, Rahul, would be too specific. We have given a broad indication. Most of our ecosystem partners are what we call anchors or manufacturers, and they belong to our 8 sectors. They are companies which have ratings from BBB to AA and we rely upon their ecosystem which includes their vendors supplying to them, distributors buying from them, and dealers buying from their distributors. We have started predominantly with the vendors supplying to these anchors and we design the programs using our technology and statistical analysis on twofold. Our underwriting scorecards which run on those vendors and then the data which these anchors share in terms of their payout cycles, what kind of things they are buying. But the main corporates with whom we are working or these anchors with whom we are working are the little fine details which we would like to maintain with ourselves.

Rahul Singhania: In this, sir, I can assume the asset quality will be better in this model as compared to the other segments that we have, right?

Shachindra Nath: We construct our portfolio maintaining at a portfolio level asset quality. What we would like to demonstrate is our portfolio level asset quality. Each of these verticals and programs has a different loss ratio projection and we balance our portfolio keeping the overall portfolio asset quality intact.

Rahul Singhania: So, it will be more or less the same as compared to the other segments, right?

Shachindra Nath: That's not what I said. I said that each of the programs have different loss ratios projected but we maintain that in terms of the portfolio construct. How much secured we will do, how much ecosystem financing we will do, how much we will do through BFSI-led partnerships, and how much unsecured we will do, that is driven by many factors. Initially, for the majority of our portfolio in our earlier years we want to do secured. Second, we have a loss ratio tolerance limit and we would like to bring our portfolio within that.

Rahul Singhania: Sir, since we are already a month down in the 4th quarter for this year, can you try to tell me how many DSAs do we present to add for the whole quarter and how many have we added in this month?

Shachindra Nath: I think the number is already given. In the opening remarks, we said we have a total of 311 which is an increase of 34%. We don't have a target for how many more intermediary or GRO partners we would add. We take periodical halts. We bring some partners on board. We make sure that they get accustomed to our technology platform. We see a level of productivity. Once that matures, then we add on next round of our new intermediated partners. We are restricted in terms of building out partners only at the physical geographies where we are present. We are present in 9 geographies. So, these partners are from those 9 geographies. We don't add partners where we don't have physical geographies. Once we add physical geographies in the coming financial years, you will see a jump in our partnership at that level.

Moderator: The next question is from the line of Kislay Upadhyay from Abakkus. Please go ahead.

Kislay Upadhyay: Congratulations on the steady quarter in the current environment and on the healthy progress in additions of GRO partners and ecosystem and co-origination partners. Sir, my question is on the economic environment that you see. You mentioned that the high-yielding segment is in more of a stress than the lower one. Can you also throw some light on which sub-sectors within our universe are you seeing having more pain than maybe others?

Shachindra Nath: We follow a very rigorous approach. Most of the lenders that we have seen, in our experience, are reactive to the market by portfolio performance. So, they build a very diversified portfolio and when there is one portfolio which is showing higher delinquency, their start and shutdown basis the portfolio performance.

We tend to believe that our approach to the market or the lending is a very proactive approach. We started with 8 sectors and these sectors are reviewed with our partners. We worked with CRISIL extensively for provision of the macro data. We look at our portfolio construct and we do market analysis. And also we do sector analysis and we do sub-sector analysis. So, we tend to believe that we will get out or halt a sector prior to when the problem hits.

To give you an example, we continue to believe the auto component as a sector on a long, 3-year basis, is still an attractive sector. But we stopped all our business in auto component 2 quarters back or probably even earlier prior to when actually it was very painful for the market. That's our approach. We continue to believe that the rest of our 7 sectors and their sub-sectors will still continue to do fairly well as long as we continue to maintain our portfolio in near prime segments. The micro market of some of them are actually under severe stress.

Kislay Upadhyay: I am sure you would be looking for early signals or possible triggers for revival in the micro SME segment across sub-sectors or even in the other sectors. What could be those triggers that can cause a revival in your opinion, sir?

Shachindra Nath: Very difficult for us. We don't tend to believe that we are experts of MSME as a business because our approach to that is we don't think that the segment has become very bad. It is just the loss ratios have gone up. Fortunately for players which are in the 25% yield segment they have absorption capacity to go from a loss ratio of 4% to 7%, which means that their liability cost would go up and they will get constraint on growth but it is not that sector is completely busted. That's our view and we continue to monitor that very very carefully. Our view is that the high-yield segment is under stress and will remain under stress. We are not seeing any green shoots to right now. It would be subject to:

1) Broad growth rate coming back.

2) Liquidity to come back wherein large banks and large NBFCs start lending them again.

3) A lot of these working capital cycles are stuck because of delayed payments from the government and so on so forth.

My personal view is that you have to wait for another 3 quarters before you will see any form of revival from the underlying economy to just revive back to a positive cash flow.

Kislay Upadhyay: Consequently, what could be the disbursal number we can see in the next 3 quarters?

Shachindra Nath: We will see the same numbers because we continue to operate. In spite of tightening and increasing our threshold, we continue to be in the prime market. I think within our sectors and sub-sectors, we will maintain the same or a little higher rate of disbursement. Our ability in the stalled capacity is for much higher rate, but we are not going there right now. Not that we have a lack of confidence in terms of the quality of the portfolio, but because we think that we are also answerable to the liability side of the market. And the liability side of the market will become nervous regarding our portfolio if we grow too fast because we don't have seasoning. That's why we would like to maintain where we are for at least 2 quarters.

Kislay Upadhyay: Finally, a small clarification. The disbursal of 1073 crores and AUM of 753 crores, the balance would be natural rundown of the short-term loans that we have given. Is that the right assessment?

Vivek Seshadri: That's right. Through the ecosystem, there is also a portion as of supply chain financing which is a shorter tenure product and therefore the gap between AUM and disbursals.

Kislay Upadhyay: So there is nothing we have sold down?

Vivek Seshadri: We have securitized this but that is still being reflected on the book because of the new Ind-AS accounting standards.

Kislay Upadhyay: And that would anyway be in your AUM in any case.

Vivek Seshadri: That's correct.

Moderator: The next question is from the line of Duby Rex from Ithought Financial. Please go ahead.

Duby Rex: Being a fintech, I think there is a heavy reliance on technology part of it. Could you throw some color on the technology development team? Is it outsourced? How many people are there in the team? A little bit more info on the COO or CTO?

Shachindra Nath: The approach we have taken towards technology; technology has 2 components – the knowledge quotient of it or the IT and the development part of it. Our belief is that we are a financial services company. There is a skill set of the people who do the development or the coding part of it, we don't need to ensure that. What has to be insured is our knowledge of providing a business solution. That's why our internal technology team is led by a COO and business analysts – a group of product and technology team which comes from deep domain expertise and who have invested or who have more than 25 years of respective domains across our 4 lines of products which we are developing. And then there is a partner vendor with whom we have a dedicated team – it varies from 30 people to 50 people – which constantly works on developing different bespoke solutions, but the IP belongs to us.

Moderator: As there are no further questions, I would now like to hand the conference over to the management for closing comments.

Vivek Seshadri: I think the message for this quarter has been that we continue to remain very watchful. We are aware of the challenges in the market but believe that the work that we have done on the underwriting, distribution, credit, technology, etc., will hold us good through these tough times. We hope to achieve a lot more in this coming quarter, especially on the co-origination side and hopefully we will have some more positive news for you in the coming quarter. Thanks a lot guys for joining the call and hope to see you again next quarter.

Moderator: On behalf of Equirus Securities Private Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.