"Fusion Micro Finance Limited Q3 FY '24 Earnings Conference Call"

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MODERATOR:	**MR. RENISH BHUVA – ICICI SECURITIES**

Moderator: Ladies and gentlemen, good day and welcome to Fusion Micro Finance Q3 FY '24 Earnings Conference Call hosted by ICICI Securities.

As a reminder, all participant lines will be in 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 touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Renish Bhuva from ICICI Securities. Thank you and over to you, sir.

Renish Bhuva: Thank you, Areeya. Hi, good morning everyone and welcome to Fusion Micro Finance Q3 FY '24 Earnings Call. On behalf of ICICI Securities, I would like to thank the Fusion Management team for giving us the opportunity to host this call.

Today we have with us the entire top Management Team of Fusion Micro Finance represented by Mr. Devesh Sachdev – Managing Director and CEO; Mr. Gaurav Maheshwari - CFO; Mr. Tarun Mehndiratta – COO of Micro Finance Business and Mr. Deepak Madaan - Company Secretary and Chief Compliance Officer.

I will now hand over the call to Mr. Devesh for his opening remarks and then we will open the floor for Q&A. Over to you, sir.

Devesh Sachdev: Thank you, Renish and ICICI Securities for hosting us. Good morning everyone and thank you for joining Fusion's Q3 Financial Year '24 Results Conference Call. I am here along with my colleagues Tarun – our COO (MFI), Gaurav – our CFO, Deepak Madaan – our Chief Compliance Officer and IR.

We had a very strong Q3 in terms of disbursements, customer acquisition, improvement in collection efficiency, NIM expansion and network expansion, which is related to healthy return ratios and robust capitalization. We had a slightly higher than guided credit cost, which I will cover in detail during this call. I request you to keep the presentation which we uploaded handy as I take you through the key highlights of the quarter.

I would like to start with Slide #5 and 6 of the executive summary:

- Our AUM has grown by 23.57% year-on-year and 6.65% quarter-on-quarter to 10,693 crore. This was supported by the highest-ever disbursements of Rs. 2,713 crore in this quarter, which is approximately 16% growth over the previous quarter.
- We have achieved this growth despite calibrating our growth in a couple of geographies, maintaining one of the lowest ticket sizes in the industry. Our diversified presence allows us the levers to grow in a very balanced manner. As guided earlier, we are on track to deliver an AUM growth of mid-20s in Financial Year '24.

- Our network has expanded to 1,242 branches across 22 states after the addition of 78 new branches in Q3, FY '24. 70% of the new branches added have been in non-top five states. We have added 1.83 lakhs new customers in Q3 and 4.23 lakh customers YTD in this financial year.
- Our total customer base as of Q3 '24 is close to 3.8 million, having grown 11.2% year-on-year. This is in line with our stated 10 to 12% increase every year in new customer acquisition.
- Another key highlight of this quarter was our credit rating upgrade also from ICRA and CARE to A+ Stable. Now we are A+ Stable from all three of our rating agencies, namely CRISIL, ICRA and CARE. Strengthened by our rating upgrade in early October and continuous engagement with our lending partners, our margin cost of borrowing further reduced by 10 basis points quarter-on-quarter to 10.45%. In the coming years, we will look to further diversify our liability mix to reduce the share of bank lending.
- As we have been guiding that our NIM will expand to 11.2% to 11.5%, our NIM now has increased to 11.54%, registering a 42 bps increase over the last quarter. We have maintained healthy NIM while offering one of the lowest rates to our customers in the sector. We will be sharing a steady-state guidance on the NIM in the Q1 of Financial Year '25, as we have been saying this in the past.
- While we continue to build capacity, we have our focus on improving our cost to income, which for the first nine months of Financial Year '24 stands at 36.5%, an improvement of 291 basis points year-on-year. There was a marginal quarter-on-quarter increase in cost to income on account of network expansion done in Q2 and Q3 which will add to the productivity in coming years.
- Last but not the least, we have delivered a PAT of Rs. 126.45 crore for Q3 Financial Year '24 which is up by 23.4% over Q3 FY '23 and our 9-month FY '24 PAT of Rs. 372.6 crore registered an year-on-year increase of 36.67%.

Now I will give an update on the collection efficiency and credit cost. Please look at Slide #8:

Our collection efficiency has steadily improved over the last six quarters with Q3 collection efficiency inching up to 97.9% and to 98.4% if we exclude Punjab.

In the Q2 call, we had mentioned about lower collections in three states apart from Punjab, namely, Rajasthan, Gujarat and Haryana. We are seeing improvement in collections in Rajasthan, Gujarat. Haryana collections have stabilized in Q3.

In our Q1 and Q2 Earnings Calls, we were one of the first companies to flag off some of the challenges we were seeing in Punjab. Punjab and Haryana states have unfortunately been impacted by external events in succession over the last few years. It started with COVID wave 1 and 2 followed by farmers agitation in Punjab that went on for more than a year and recent rains and floods, what we have mentioned in Q1, created an adverse impact on our customers' ability to generate livelihood versus pre-COVID times.

To add to the immense impact that these events created on income generation activity of our borrowers, last few months there have been some mischievous campaigns in Punjab misleading on innocent customers with illegal and unfounded claims of waivers. Due to the increased stress, which is visible now, we have specifically called out the share of Punjab portfolio in our overall AUM in Slide #9. As of December '23, the share of Punjab in our overall AUM stands at 3.6% and collection efficiency is at 84.4%. Our January '24 Par 60+ in Punjab has increased to around 20%. Our collection efficiency and Par 60+ ex of Punjab remain within a healthy range.

We are taking many steps which have been mentioned in the slide, even the MFIN has met Finance Minister of Punjab to apprise of all the issues which are coming in especially from some of the districts. We have stopped fresh disbursement in Punjab as we have mentioned in Slide #9. We are in a wait and watch mode and whatever I think the drop in the collection efficiency, has already happened in January, now it has more or less stabilized at a certain level.

Moving to Slide #10 our GNPA as of Quarter 3 Financial Year ‘24 stands at 3.04%, net NPA at 0.77%, which has increased from Q2 majorly because of Punjab. Our credit cost net of recoveries for Q3 stands at 0.94% and we expect to close the year with a net credit cost of up to 3.5%, which will take care of major impact of this state. We have progressively shifted ~80 crore of assets from Stage-1 to Stage-3 to take care of potential slippages.

In our previous calls, we had guided that we are creating management overlay as a buffer for exceptional geographical issues. Accordingly, in Q3, we have released approx. 20 crore from management overlay to normalize the impact of stress caused by Punjab. The management overlay as of December end stands at 41.5 crore.

It is important to note that despite elevated net credit cost of 2.47% in 9 months Financial Year ‘24, our 9 months FY '24 ROA at 4.87% and ROE at 19.75% remains healthy. This demonstrates the robustness of our business model.

Now I would like to update on our geographical diversification, branch mix, average ticket size, performance and key operation parameters and brief on our MSME business:

Diversification has been one of our key strategies for growth since inception which has helped us to grow our presence in 22 states across 1,242 branches as of Q3 Financial Year ‘24. We continue to remain committed to our diversification journey through expansion in newer states like Karnataka, Andhra, and Telangana.

Over the last year, the concentration of our top five states has increased to 70.4%. This is an account of good traction and healthy portfolio, we have seen in these states and being an established player gives us better scalability and productivity. However, for the long term, we remain steadfast on our strategy of diversification as shared earlier.

As highlighted in Slide #19, we have opened 156 branches in nine months Financial Year '24. We are targeting to add approximately 200 branches in Financial Year '24.

While on the point of branch network, I wish to take you to Slide #23 where you will see we have very good mix of vintage and new branches, which is very strong operating lever for our future growth. 510, which is 44% of our branches are less than three years old which contributes to just 29% of our AUM. This will improve as the branches get seasoned and aid our AUM growth. Our average outstanding per borrower stood at approx. Rs. 27,200 in December '23. As per latest MFIN data, this is one of the lowest in the industry.

Slide #21 captures our key productivity metrics. Our GLP per branch has been following a consistent growth trajectory and now stands at Rs. 8.9 crore per branch as of Q3 Financial Year '24 versus Rs. 8.8 crore as of Q3 Financial Year '23. GLP per RO at Rs. 1.3 crore, clients per branch of 3,260 remain one of the best in the sector.

Moving to Slide #37, which gives an update on MSME vertical, which was started in December 2019 with a vision of building credit underwriting capabilities to tap into the potential of missing middle, mapping adjacencies and serving MFI customers, which are moving up the value chain. Happy to share that this book now has a portfolio of Rs. 461 crore, which is 4.3% of our overall AUM. approx. 60% of this MSME book is secured.

We have been guiding that we would like to maintain portfolio mix of 65% to 70% secured and 30% to 35% unsecured in MSME to balance risk and return and we are absolutely on track. We are confident of reaching this mix in the next three quarters. We would like to mention again that we will share our broad growth strategy on both verticals in Q1 of Financial Year '25.

Having shared the highlights of our Q3 Financial Year '24 performance with you, I would like to reiterate again, our goal always is to maintain a long-term view on building our businesses, setting a strong and consistent growth platform, transparency and sustainability. Thank you very much.

Gaurav Maheshwari: Good morning everyone. Would like to give some key highlights on Q3 FY '24.

The core interest income of the company has increased by 8.70% on a quarter-on-quarter basis and on a year-on-year basis, it is 28.50% growth. The total income has also increased by 7.35% on a quarter-on-quarter basis and 31.45% on a year-on-year basis.

Our marginal cost of fund has further reduced by 10 bps on a quarter-on-quarter basis and 75 bps on year-on-year basis aided by our focused approach on optimizing the cost of funds. Our endeavor would be continuing to work on optimizing our cost of fund.

CARE and ICRA have also upgraded our long-term rating to A+, followed by CRISIL which had done it in the month of October. This would help us in tapping the capital market and ECB exposure to diversify our funding base.

The NIM for the quarter increased by 42 bps from Q2 and it has increased by 123 bps on a year-on-year basis. It is as per our guidance provided earlier. As on 31st December, the PPOP is INR 260.26 crores, increased by 41.62% on year-on-year basis and 7.64% on a quarter-on-quarter basis.

The cost to income has marginally increased by 39 bps from 36.41% in Q2 FY '24 to 36.80% in Q3 FY '24. The operating cost % increased by 24 bps on a quarter-on-quarter basis to 5.85%. This increase is due to opening of 78 branches in this quarter pan India. Also, due to the addition of 1,155 additional manpower in this quarter. Operating cost for MFI business is 5.37% and MSME business contributes 0.48% for the quarter.

Please refer to Slide #10. The ECL as on December 31st is INR 311.85 crore which includes management overlay of 41.50 crores. The overall coverage stands at 106%. The net credit cost for 9 months FY '24 stands at 2.47% on average on book portfolio. For the quarter, the credit cost is 0.96% on a closing portfolio. We are confident for closing FY '24 with the net credit cost of up to 3.5%.

The company has done write-off of 81.31 crores in Q3, which is 0.84% on the closing portfolio. Due to this write-off, we have de-recognized the interest amounting to INR 18.75 crores. The management overlay we have created till last quarter was 61.48 crores. As mentioned in our previous call, it was mainly created to mitigate the impact of any future risk.

During this quarter, the company has decided to use the management overlay up to 20 crores for writing-off 270 plus DPD largely pertaining to Punjab. We have provided, as Devesh has mentioned, from Stage-1 to Stage-3, there is a shift of a portfolio. By this shift, we have provided approximately 16% of the Punjab portfolio to the provisioning. The gross Stage-3 stands at 3.04%, which is the gross NPA, and the net Stage-3 is 0.77%. This is from the financial side. Thank you.

Moderator: Thank you very much. We will now begin the question-and-answer session. First question is from the line of Piran Engineer from CLSA. Please go ahead.

Piran Engineer: Just a couple of things. One is any further recognition left for asset quality issues in Punjab or maybe the neighboring state of Haryana?

Devesh Sachdev: Yes. So, Piran, that's what, one, we have front-loaded some of the pain. But if you see our guidance is up to 3.5%. So, our endeavor is that whatever the pain, we take it in this quarter and in Q4, so that we can start the new financial year on a clean slate.

Piran Engineer: And this 3.5% credit cost, does it include any more drawdowns from the overlay buffer?

Devesh Sachdev: We are not hoping for that. We would like that whatever we have dipped in the management overlay does not increase in Q4. We would not like to use it now in the next quarter.

Piran Engineer: That's helpful. And secondly, some of your competitors have passed on yields to their customers by about 50, 60 bps. Any such thought process from our front on this?

Devesh Sachdev: We are very clear, we have been saying this that once we see that the pivot happens, we are reaching a certain steady state of NIM, ROA and ROE, once we see that there is some benefit which is coming from the rate of interest or cost of fund, we would definitely like to optimize cost to customer, sensitivity and the shareholder value. We are today amongst one of the lowest in terms of cost to the customer in the sector. So, right now there is no such plan but once the pivot happens, we will look at it and in Q1, we have mentioned that we will give some guidance. But right now, there is no such plan.

Moderator: Thank you. Next question is from the line of Raghav Garg from Ambit Capital. Please go ahead.

Raghav Garg: Just I was listening that you are still expecting some kind of slippages in 4Q from Punjab and Haryana. And if I look at the credit cost for the nine-month period, I think that comes to on an annualized basis somewhere around 3.5% or slightly more than that, as per my calculations at least. How is it that you are guiding for a 3.5% credit cost for the full year? Shouldn't it be slightly higher unless you are expecting that the credit cost will normalize to 3, 3.1% in 4Q? Is that the case?

Gaurav Maheshwari : No. Raghav, what we need to see that how the situation is developing in the state of Punjab. So, if we see the last 10 to 12 days of collection patterns, it is getting stabilized. As Devesh has mentioned in his earlier remarks, that we are engaging with the ministry level at the Punjab administration. So, they have extended some help. So, we are hoping that the situation will not deteriorate. If there is a deterioration, our Punjab portfolio is not large enough to have a further major pain . So, that's the way we are looking at things. So, the situation is evolving. And January collections have stabilized now in the last couple of days, as I have mentioned. So, that is why we have given upto 3.5% of credit cost as the guidance.

Raghav Garg: Gaurav, I think, thanks for that explanation. But the only question was that, do you expect that your credit cost will be around 3% in 4Q? Because your full-year guidance seems to imply so. I am asking whether your 4Q credit cost will be around 3%, because your full year guidance of 3.5% seems to suggest so.

Gaurav Maheshwari: No. So, Raghav, that is what we are saying, that the situation is evolving in Punjab. So, it would be very difficult to say that it would be a 3% cost. But what we can assure you is that, the major pain is being taken care in this quarter, if there is an incremental slippage of maybe some sort of portfolio. And second, if you see that the number which we have given is of December, , and there is a rundown in January which has already happened in Punjab portfolio. The number, which is 382, has run down to 362 already because we are not doing incremental disbursement, and apart from that, the situation is getting stabilized. So, that is why we have restricted to slightly on a higher side on the credit cost at FY '24.

Raghav Garg: And just one last very generic question. Any other pockets of stress that you would like to highlight outside of say, north or anywhere else wherever you look?

Devesh Sachdev: No. No.

Raghav Garg: So, next year should be a largely normalized credit cost year for you of around…

Devesh Sachdev: Absolutely. That will be our endeavor. We were actually moving on the right direction, though there was some hump. So, we as a transparent company, we thought let's front load this in this quarter. And if there is anything we can take in the Q4, we expect a normalized credit cost starting next financial year.

Raghav Garg: And also, can you give us your top five states break up in terms of the loan book outstanding? Is that something that you can do?

Devesh Sachdev: Yes. So, it says 70.4% in the top five states.

Raghav Garg: No, what I meant is your top five states, can you give us a loan book breakup by each state of the top five states?

Devesh Sachdev: By percentage?

Raghav Garg: No, by absolute amounts.

Devesh Sachdev: Yes, we can give that. So, UP is 2,326. Bihar is 2,104 crore. Odisha is 1,217. Madhya Pradesh is 969. Tamil Nadu is 685. These are our top five states.

Moderator: Thank you. Next question is from the line of Abhijit Tibrewal from Motilal Oswal. Please go ahead.

Abhijit Tibrewal: I was away for some time. So, I mean, excuse me if you have already answered this. I can always listen to the recording. But just wanted to understand, have you explained already what exactly is the nature of problem today in Punjab and Haryana? Why I ask this is when we read about this on media, right, I mean, we get to hear something else when we kind of do some channel checks, try to understand that from MFIN, we get to hear something else. But given that you are going through this, right, if you could just elaborate on what exactly is happening in Punjab and Haryana?

Devesh Sachdev: So, look, Abhijit, we have already mentioned it, but again, no problem. I will just again mention this. Look, post-COVID-1 and COVID-2, Punjab, Haryana and Rajasthan and these states were slightly slow in coming back. Okay? What happened was, after that, there was a big farmer agitation, we all know, which hit Punjab and some parts of Haryana. once this subsided, then the floods hit, which we have highlighted in Q1.

Now, the situation in Haryana has stabilized. We do not see any risk. Also, let me just tell you, our Haryana portfolio is 256 odd crores, which is around 2% of our book. Punjab is 382, which has now come down to 362. It's close some 3% portfolio. Punjab, specifically in some of the districts, after this flood issue, some mischievous elements started doing this whole loan waiver campaign, by which people stopped paying. Actually, our boys were not allowed to even enter some of the villages. Collection efficiency has come down to 84% as we have mentioned in Slide #9 in Punjab.

So, that's the situation. We have 55 branches. We actually had 42. 13 branches were split to increase the monitoring. We actually calibrated our strategy of going slow in Punjab, and then we first stopped the disbursement in the impacted branches. Then finally we took a call-in end December to actually stop disbursement in every branch. Now we have strengthened our, as we mentioned tele-calling, overall infra of our collection. We are reaching out to customers and MFIN, we have met the Finance Minister of Punjab, and saw the Finance Minister is trying to help us.

So, also what we have seen is that whatever the collection dip was there, now that has got stabilized. So, that is what gives us confidence, and that is the reason we front-loaded some of the pain, and we are confident that we will be able to manage the credit cost within the 3.5% for this financial year.

Abhijit Tibrewal: This is useful. And sir, have you also kind of shared, I mean, sir, before I move to the next question, just wanted to kind of reconfirm when you said some mischievous elements after the flood had started this loan-waiver campaign, fair to assume here that this loan-giver campaign does not have the support of the political machinery of Punjab there?

Devesh Sachdev: No, not at all, not at all. Even the Finance Minister was also surprised to see. And let me also tell you, this loan-waiver is not only for micro finance, but for all loans. It is for all loans, all bank loans, every loan. So, it is not specifically for micro finance. Micro finance customers being vulnerable, so these customers are misled. Otherwise, it's not only for this thing, and there is no political support, what we know, for any party for this kind of campaign.

Abhijit Tibrewal: This is useful. And sir, maybe one last question from my side is, have you also shared the Stage-1, Stage-2, Stage-3 of the Punjab portfolio, which you said is around 360 crores now? Have you also given the split of the Stage-1, Stage-2, Stage-3 of the Punjab portfolio?

Gaurav Maheshwari: So, we have not given the split of Stage-1, Stage-2, Stage-3 for Punjab. But we can provide you if it is being required.

Devesh Sachdev: We will provide you separately.

Moderator: Thank you. Next question is from the line of Shweta from Elara Capital. Please go ahead.

Shweta: Couple of questions. So, Tamil Nadu also forms one of your top state exposures and one of our largest peers here has seen impact of floods there. So, any such troubles are asked in that particular state?

Tarun Mehndiratta: So, see, Tamil Nadu, yes, there were rains and floods and there have been series of rains and floods. But actually, we have about 99 branches in Tamil Nadu and only about 19 to 20 of those branches were in the areas where we had experienced these. So, for us, yes, there were very marginal phases of impact, but the Tamil Nadu portfolio has bounced back. And actually, we have seen that not only has it stabilized, it started to also inch upwards to improve. So, really for us, I think Tamil Nadu is behind us now in terms of whatever little impact that it had because it was a very small number of branches that we had impacted by rains.

Shweta: Secondly, in terms of yields, so while you did mention that there will be recalibration of yields going forward as you move towards optimization, but what is the own book yields today and what is the sort of IRR for the customer?

Devesh Sachdev: The average is around 23%.

Shweta: And IRR would be?

Gaurav Maheshwari: So, the IRR would be, you can add 1.25% as the LPF. So, you can calculate that XIRR,

Devesh Sachdev: That is for two years.

Shweta: Sir, last question is, so you made a briefing mention that 16% of Punjab provision because there have been movements between Stage-1 to Stage-3. I sort of didn't get that clearly. Can you just repeat?

Gaurav Maheshwari: So, Shweta, because in a Stage-1, you have a lesser provision requirement as far as the ECL model is concerned. So, because of the situation being demanding, we have shifted certain portfolio from Stage-1 to Stage-3. So, earlier this provision was not as high. It was as low as like maybe 4% of the total Punjab portfolio. By moving that approx. 80 crores of portfolio to Stage-3, this number now increased on a closing portfolio to 16% because a larger share is now sitting in the Stage-three. So, that is why it has given us an amount of 16% on the Punjab portfolio as a provision.

Shweta: And one last question. Sir, what is your ROA target for next quarter given that you have already frontloaded with Punjab impact? Also, what are you looking at cross cycle ROA over the next three to five years?

Devesh Sachdev: Shweta, we have been guiding this since we went to the street first time 4.25 to 4.5% ROA guidance cross cycle and ROE of 18 to 20%. That is what we have been guiding consistently over the last 18 months.

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

Rajiv Mehta: Congrats on delivering good results despite the issues in Punjab and thank you for taking my questions. So, the first question is, sir, what scenario of collection efficiency in Punjab will make us miss our credit cost guidance? So, can you mention the level of collection efficiency below which we will miss our guidance of credit cost?

Devesh Sachdev: No, look, we have already done some estimation. This all decision of front loading was also taken looking at the January numbers. So, I can tell you from collection efficiency 84% in December, there was a 5 to 6% drop in the first few days of January. After that, it has stabilized. So that's what we are trying to do as a transparent company that we have seen that, and I am hoping that the situation will not go down from here. Also, Rajiv, overall, there is run-off which is happening on the portfolio, there is a 20 crore runoff that's already happened. As Gaurav has mentioned, 16% of the Punjab book has already been covered under this. So, I don't see any challenge now.

Rajiv Mehta: And hypothetically, if the situation gets arrested at the current collection efficiency, then in that case, would any additional provision be required in that case, what we have budgeted for already in the credit cost, but would that materialize?

Devesh Sachdev: I think let's wait for Q4, we will look at this quarter and we will see, but otherwise, whatever we estimation we could do looking at the collection efficiency, customer behavior and the portfolio and the loss estimation, I think we have already factored in this quarter and the next quarter, Rajiv. But yes, it is always a moving number, but we are hopeful and confident that I don't think we will go much beyond this number.

Rajiv Mehta: And on this, you know we have also mentioned in one of the slides that we have stopped customer addition in whole of Punjab. So, would it have any impact on the momentum that we have seen in Q3? We have seen good momentum in customer addition, disbursements. Would there be any impact of it or should we assume that the momentum in customer addition, disbursements, which has revived, will keep on continuing?

Devesh Sachdev: It will keep on continuing, Rajiv, that's what I have mentioned in my commentary. We actually had to calibrate our growth in three states. We went slow in three states. In spite of that, looking at on our overall network of our branches in Q3, we could still grow. We have done overall disbursement of ~2,700 crore. So, that has already been factored in. Other branches will contribute. So, the momentum will not break.

Rajiv Mehta: And then last thing on the new customer being added, the profile in terms of we being the first or the second lender, that profile is intact in terms of the uniqueness, the unique relationship with the borrower?

Devesh Sachdev: More or less similar. Rajiv, we have mentioned earlier also that every six months we will share the data. We shared the data in September. So, we will share again after the Q4 results. We will take a fresh dump, but more or less there is not much change. But more granular data which we have already provided after the September result, we will provide again after Q4.

Moderator: Thank you. Next question is from the line of Pranav Gupta from Aionios Alpha Investment Management. Please go ahead.

Pranav Gupta: Congratulations on a good set of numbers despite the problems in Punjab. Just a couple of questions. So, if you look at disbursement ticket size, you had mentioned last quarter as well that we have taken a change in stance and we have started to increase the first cycle disbursement ticket size slightly albeit it is lower than the industry. But when I look at this increase over the last few quarters, is it a function of the changes that we made or is it more a function of our customers moving from say a first cycle to a second cycle or second cycle to third cycle? How should one look at that?

Devesh Sachdev: One, we have not done any change in this quarter. Whatever change we have previously communicated stands. We have not tinkered with any loan sizes and cycles after that. But you are right. This is a combination of both customer retention and some combinations. It is a calibrated thing. So, that's it. It is a combination of both.

Pranav Gupta: And just in continuation to that question, if you look at the expansion that we did, that we have done over the last nine months, we have added almost 150 odd branches. Two questions there. One is, can you talk about any apart from say new states we added like Telangana and AP, have we looked at deepening presence in any specific states? And this quarter, we added almost 1,200 odd ROs as well. So, again, is it state specific? Is it a deepening presence in any particular state? Or is it just a broad-based increase? And lastly, just could you give the breakup of all of these 156 odd branches added, how many of them were through splitting and how many were new branches?

Tarun Mehndiratta: So, just to answer the first question, the expansion, like Devesh had mentioned earlier, 70% of the expansion has come in non-top 5 states, right? So, it tells you that we have also looked at deepening some of the states which were outside of top 5, but significantly in our earlier discussion in the previous quarters, we said about our forays in AP and Telangana and also the fact that we had entered Karnataka. So, 64 branches out of these 156 came into these 3 states.

And other than that, we looked at deepening some of the existing states. So, that is really how our expansion combination has been.

Now looking at this question of saying the split branches, so yes, in our overall portfolio, if we look at it today, close to about 130-140 branches are what we had typically split more from a monitoring standpoint. And that is a strategy, which Devesh had mentioned, that consciously, we had also done in Punjab in early part of this financial year, more from a monitoring standpoint. So, 13 branches we had split just to be able to monitor more intensely the portfolio. But overall in the country there are about 132 branches which are split out of the total 1,155 MFI branches.

Devesh Sachdev: Because, you know, Pranav, if you look at our branch per district, it is around 2.66. If you compare with the sector, it is more. As we mentioned, we are now in the deepening strategy other than the new states which we have entered. We will keep on splitting the branches which crossed a certain AUM size or number of customers.

Pranav Gupta: So, just one last question from my end. So, I mean, through COVID as well, we have continued our expansion in the new states, the new geographies, continued to open branches and that has aided us in acquiring new customers through the COVID period as well while the industry was sort of subdued. When we look at the last 12 to 15 months, we have again continued with that journey of expansion, like you always mentioned in trying to sort of diversify geographically. Is it fair to assume that this expansion now and the branch split that we have where 41% of branches are still contributing relatively lower share into AUM, should one assume that this should impact cost ratios positively going forward as operating leverage kicks in over the next, you know, over a more longer term, over the next two to three years? How should one look at the cost ratios?

Devesh Sachdev: Absolutely, absolutely. Pranav, look, that's what we have been saying that there are two, three things I would like to mention here that one, standalone micro finance or operating expenses or you see cost to income, we are already very, very competitive. We will be, if I take out the MSME piece, we will be around 32, 33% cost to income. So, that is one.

Second is, as we are mentioning, we are trying to calibrate between the future and managing the cost. We are calibrating our overall strategy even on the number of customers handled by the field officer to have a better control of the portfolio. So, you are right. We will optimize this thing, but yes, over the next two to three years, and also we are investing. We will be adding good number of branches even the coming year, which we will give some guidance in financial year, in Q1 of '25.

However, we will try to balance both cost to income and the growth and everything. And yes, over a period of time, you will see once these getting stabilized and the branch expansion will be to not that kind of percentage, that level, you will see operating levers, you know, playing out.

Moderator: Thank you. Next question is from the line of Umang Shah from Kotak Mutual Fund. Please go ahead.

Umang Shah: Just a couple of them. One, on the credit cost, right, I mean, let's say on a more steady-state basis, when you guide for a 425 to 450 basis points of ROAs, I mean, what are the credit cost assumptions that you are digging in and more closer for FY '25, would you like to guide for any credit cost number?

Devesh Sachdev: Yes, Umang, hi, good morning. So, we will guide for this in Q1 '25, that what are the kind of overall cross-cycle ROA, ROE, credit cost, we will achieve. But yes, endeavor would be to really be or more, much better than what we have achieved, but you will see better numbers going forward, Umang. We will give some guidance, but we are very confident of having a better number, and there are some bumps in any journey. But I think the benefit we have, as a diversified company is, we are able to even calibrate some of these things. We are able to calibrate even the issues in some of these states in a much better way and still grow. But coming to your point again, we would definitely like this to be better, credit cost to be much lower, but we will give a guidance in Q1.

Umang Shah: I appreciate that, Devesh. I was coming from the point of view that clearly in our earlier conversations, we have spoken about a 4.5% ROA. You guys are well above that. But clearly at that point of time, the thought process was that at the same time we would be building some buffers on the balance sheet. Now I appreciate that clearly, Punjab is a one-off sort of a situation. But given that we are widely diversified compared to our peers, right? Given that Punjab is a classic example, there could be a possibility that maybe at regular intervals, we might have a marginal state which can cause some troubles to us and probably that can keep our credit costs elevated for a much longer period. Is that a possibility? I know it is difficult to foresee at this point of time, but probably should we assume that that is a cost of diversification?

And also, the second part to it is, I was just looking at the vintage curve of our branches, right? I mean, clearly the share of younger branches within the overall mix continues to go down, but on the AUM or the POS side, clearly, we are actually getting more concentrated in top 5 states, right? So, I am not too sure how to read this whole diversification thing both from growth perspective as well as from an asset quality perspective.

Devesh Sachdev: One, so coming to your point, look, I understand that top 5 states are 70%, but yes, because of this hump, because I can tell you, Umang, there was a point where if I can talk about 2 years back, 15, 18 months back, Punjab was a top 5 state for us. So, look, there is no straight answer, but in our experience, diversification always helps- if you are diversified both from the growth, from the risk perspective, I think, and that is what we are seeing even in this situation, that even when there is an issue in one state, we are able to calibrate better, but I will still stick to this diversification strategy.

Also, Umang, if you see even in Punjab, it is basically some districts which have got impacted. So, it is not the full state. So, I think we have an overall district strategy of not being more than 4% in any district. Highest district today is 1.59%. So, yes, I think we are very confident this strategy will play out.

Coming again to your point that some other state can have trouble, look, definitely nobody can predict it. However, I can talk about two, three things. One is that, that is the reason we started making management overlay and that is why, because it is a exceptional situation, we dipped into management overlay. Whenever there is an opportunity, we will keep on building this management overlay. That is one.

Second is, RBI has since 2022 mandated for a risk-based pricing. So, we are able to have different yields in the states where we see the risk is higher which will make sure that we are able to deliver the cross-cycle ROA, ROE, which we are promising.

Umang Shah: And just one last question now on this yield part. I think you already in some of the previous questions, you have already answered this part. Just wanted to pick your brains again between this whole growth and margin dynamics, right? So, I mean, some of the other micro finance NBFCs have started cutting yields. Now clearly to begin with, we were, and we are kind of still competitive even at our current yield level. current yield level, but do you foresee that at some point in time pressure on yields might start coming through and assuming that if we don't pass on the benefits of operating leverage, probably growth might take a backseat, or you are confident enough to maintain this whole growth and margin mix where we are today? That's my last question.

Devesh Sachdev: We are confident. I have already answered this point earlier that we are going to optimize between shareholder, customer and the sensitivity of the regulator. We did not burn the ocean when the pricing was deregulated. We are one of the lowest cost to the customer. We will optimize it whenever there is any pivot which happens, but we will be able to maintain this whole balance between growth, margin and ROAs. So, we are very confident. I don't think, Umang, there is any question mark on this point.

Moderator: Thank you. Next question is from the line of Himanshu Taluja from Aditya Birla Sunlife AMC Limited. Please go ahead.

Himanshu Taluja: Just a few questions at my end. Sir, when we look at the collection efficiency excluding Punjab of 98.4, congratulations for that. This is what you are trying to think in the previous quarter that we are going to deliver some improvement. That is the path clearly visible. Sir, if I look at your net NPL addition excluding the Punjab area impact of approx. 80 crores, which looks around 50 crores, 50, 55 crores, which is meaning 2 to 2.2% of the slippage ratio. Do you think with this collection efficiency of 98, above 98, this is a more sustainable nature of the slippage ratio one should expect?

Gaurav Maheshwari: So, Himanshu, to address this question is that still there is a pool which is available beyond 90 plus, which might get eligible for a write off, but the range would be between 1.75% to 2% of gross NPA, which is sustainable. As we have mentioned previously that this business is having a steady-state gross NPA between 1.5 to 1.8%. It is going to be continuing.

Himanshu Taluja: Second question I need few clarification on the Punjab. Have you completely stopped the incremental disbursement to the entire state of Punjab or only to the few affected districts? And how do one should see this 380 crore of Punjab portfolio? Is it going to slow, will be a declining trend from here?

Devesh Sachdev: So, Himanshu, we have stopped complete disbursement in December. As I mentioned earlier, the portfolio, which was 382 crore as of December, has already come down to 362 crore. We are right now in a wait and watch mode. If we see that there are customers which have been paying us well, they want to renew the relationship, we will definitely would look at it, but for that we have to be confident that the situation is improving. Otherwise, right now, it is at a wait and watch mode and the whole focus is only on engagement, working with administration and collection.

Himanshu Taluja: And sir, in this nature of the business, when you slow down or stop the disbursement, you generally tend to see slightly more slippages happening from here. Do you envisage any risk from the remaining 360, and if I include this eighty crore of the Stage-3 of the remaining portfolio, do you envisage any risk of further slippages from there?

Devesh Sachdev: No, that is what I am saying that we have taken this decision based on looking at the last 10 days collection efficiency in the month of January. So, we do not see that the collection efficiency will go down from there. It is more or less stabilized at a certain level which is 5-6% less than what we have mentioned in our slide. So, we are hoping, but you are right. I mean, you have to be very mindful. Situation is fluid, but we are keeping an eye on it. Yes, but that is the call we have to take because the situation was slightly exceptional. But yes, we will update if there is any other development.

Himanshu Taluja: Lastly, just the last question, how one should see what is your guidance on the growth from here of the entire portfolio? Do you still expect to deliver for FY '25 as well around 25% sort of a growth?

Devesh Sachdev: That is what we have mentioned. But mid-20s, yes. Mid-20s is the growth which we have been guiding and how both the verticals, both MFI and MSME will grow, we will give a more clear granular information in Q1.

Moderator: Thank you. Next question is on the line of Renish Bhuva from ICICI Securities. Please go ahead.

Renish Bhuva: Sir, just one question from my side. This is more related to Punjab again. So, let's say, do we understand the state level issue and it's not a company specific issue, but as a company, what are the corrective measures we are taking to make sure that collection efficiency at least holds up at current level and it should not deteriorate from current level? I mean, as a company, what we are doing to sustain this collection efficiency?

Devesh Sachdev: So, one, we have split the branches. We have strengthened the field. Telecalling is happening and through various methods, we are trying to reach out to the customers to actually educate them about these mischievous elements. Dedicated collection is happening. So, I think all whatever we could do, we are trying to even use some of the good customers to talk to the other customers that look, I mean, this will actually impact their Credit Bureau score.

So, we are doing, as all these steps are happening, other than what is happening at a sector level, there has been some advertisement which has come out from the sector from MFIN. As I mentioned to you, MFIN delegation has met Finance Minister. We could see some action soon, but yes, that's what. Yes, it is also, if you see, Renish, in Slide #nine, we have mentioned all this.

Renish Bhuva: Yes, but so I just wanted to get a sense at the ground level. So, let's say, what is the center attendance or let's say, do we have allocated any senior resources to look after only Punjab collection? So, just wanted to have some granular details about it, if you can share.

Tarun Mehndiratta: Yes, Renish. So, now there are two Fusion Micro Finance senior level veterans along with a senior level AVP regularly monitoring the situation in Punjab. To add to what Devesh just said, the entire dedicated collections team, as well as the business team, is focused on not only looking at daily collections, but also going across and meeting up with customers. We are also using local level people who have been with us over the last few years in terms of impressing upon the others about this mischievousness of this particular scheme and the impact it may have on their credit discipline and Credit Bureau scores and so on and so forth and future possibility of getting loans from any finance company or bank for that matter. So, there is complete focus on ensuring that there is a normal kind of discipline coming in. Like Devesh mentioned, last 10 days we have seen decent stabilization and we hope with all the efforts that we along with MFIN are making, that will start showing results in due course.

Renish Bhuva: Yes. I mean, that was my last follow up. So, basically, whatever we are doing at the ground, do we see some sort of initial improvement at the collection or center readiness level, maybe in first half of February?

Tarun Mehndiratta: So, like I said, so there has been stabilization. Now in such a situation, we expect, people had taken a decision, which they were misled. So, coming back to normal, they will also come back a little bit more slowly and gradually. But the good part is that we have not seen deterioration in the last 10 days. That's what Gaurav also mentioned in his opening remarks about Punjab. So, that has been a positive.

Moderator: Thank you. Next question is from the line of Rajiv Pathak from GeeCee Holdings. Please go ahead.

Rajiv Pathak: Just one question on the vintage. So, if you look at our branch vintages over the past two years, I am taking a point of view that two years plus kind of branches have gone up by 40% in absolute numbers. Similar is the increase in the number of customers that we do. But the average ticket is going up by 20%. And it is also evident from the fact that your branch contribution of the two years plus to the portfolio in terms of the number of branches would be around 72%, whereas the contribution is 87% in terms of the AUM. So, slightly there has been some conservativeness on the ticket front and rightly so. What could this be attributed to? Would it be the shift in the mix of the top five states or you being conservative in some of the geographies and that being the case, if things turn out to be normal in FY '25, do you have a case for a slightly higher ticket for your vintage customers, you know, and feeding into the cost efficiencies on this part?

Devesh Sachdev: So, if I look at this break up, I think more or less, if you see between two to three years branches are 185, they contribute around 16%, more than three years are contributing 71%. More or less, that has been the ratio. But coming to your point, Rajiv, look, right now, we are calibrating our strategy in terms of how we retain our customers, especially when customers are maturing. And so, we will share some of these details in Q1 of '25. But keeping in mind our broad philosophy of marrying risk and growth, I think that is what we will keep in mind. And anything which we will do to make sure that portfolio quality definitely remains impeccable. So, that will be our strategy.

Moderator: Thank you. Ladies and gentlemen, that was the last question of the day. I now hand the conference over to management for closing comments.

Devesh Sachdev: Thank you everyone. We remain committed for a long term. I think that's what the kind of building blocks we are building. Thank you.

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