“Poonawalla Fincorp Limited
Q2 FY2022-2023 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to the Q2 FY2022-2023 Earnings Conference Call of Poonawalla Fincorp Limited.

As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. To ask a question participants may press "*" then "1". 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 will now have the conference over to Mr. Hiren Shah – Head Investor Relations, Poonawalla Fincorp Limited. Thank you, and over to you, Sir!

Hiren Shah: Thank you, Rutuja. 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 September 2022. We will take this opportunity to update you on the recent developments in the industry as well as Poonawalla Fincorp during the quarter.

To discuss all this in detail, I have got with me our Managing Director, Mr. Abhay Bhutada, Managing Director of Poonawalla Housing Finance, Mr. Manish Jaiswal, and other senior management officials and myself, Hiren Shah, Head of Investor Relations.

Now I would like to request our Managing Director, Mr. Abhay Bhutada to brief you all about our company's operational and financial performance along with developments for the quarter ending September 2022. Over to you, Sir!

Abhay Bhutada: Thank you, Hiren. Hello, everyone. I welcome you all to the Poonawalla Fincorp Q2 FY2023 earning conference call. Trust you are all doing good. On behalf of entire Poonawalla Fincorp team, I wish you all a very Happy Deepavali.

Let me take you through the key highlights for the quarter. Q2 has been an excellent quarter with differentiated strategy and execution excellence leading to all-round performance across business growth, improved credit quality, and profitability. It was a quarter marked by highest-ever organic disbursement, customer acquisition, lowest GNPA and NNPA, and highest ever PAT and ROA. Also, our long-term rating was upgraded to AAA/Stable by CARE Rating Agency. This sets the momentum for an even exciting second half and beyond. All this is a testimony of leadership team's relentless effort and focus towards achieving the management vision and creating value for all our stakeholders.

During the quarter our PAT increased to Rs. 163 Crores, up 71% YoY, 16% QoQ. Our ROA reached highest ever level of 3.6% at a consolidated level, an improvement of 102 bps YoY, 24 bps QoQ. Our AUM stood at Rs. 18,560 Crores, up by 22% YoY and 5% QoQ. The focused AUM growth was even higher at 56% YoY, 11% QoQ, as fresh disbursement grew by 44% YoY and 8% QoQ to Rs. 3,721 Crores. NIM was at 9.8% in Q2, increase of 77 bps YoY and 35 bps QoQ. NII stood at Rs. 446 Crores, an increase of 33% YoY and 12% QoQ, while the average cost of borrowing was contained at 7.12% for the quarter, despite the 190 bps cumulative repo rate hike since May 2022.

In terms of asset quality, we aligned Stage 3 classification with revised NPA definition as per the RBI. The aligned GNPA reduced to 1.52%, down to 59 bps YOY and 67 bps QoQ, while net NPA reduced to 0.83%, down 118 bps YoY and 13 bps QoQ. I am happy to share that this is the lowest GNPA and NNPA levels in last 38 quarters for us and amongst the lowest in the NBFC space. This is given by our chosen customer segment, the high credit bureau score portfolio, superior collection infrastructure, close monitoring of early warning signals, coupled with proactive credit policy changes.

At Poonawalla Fincorp standalone level, our PAT increased to Rs. 130 Crores, up by 76% YoY and 5% QoQ. Also, our AUM grew by 17% YoY and 4% QoQ to Rs. 13,161 Crores. ROA standalone was at 4%, this is the highest ever ROA for the quarter ending September 2022, which is an increase of 131 bps YoY. The focused AUM, which is 88% of our total AUM, grew at 68.5% YoY, 12.5% QoQ. The entire disbursement during the quarter was through organic route, which grew by 42% YoY to Rs. 3,110 Crores for Poonawalla Fincorp at a standalone level. The NIM stood at 10.4% with an increase of 55 bps YoY, 3 bps QoQ. GNPA was at 1.77%. It is a reduction of 302 bps YoY, 91 bps QoQ, while net NPA stood at 0.94% with reduction of 132 bps YoY and 17 bps QoQ.

The affordable housing finance subsidiary PAT grew by 75% YoY and 8.3% QoQ to Rs. 33 Crores, while the AUM stood at Rs. 5,612 Crores, which is up by 31% YoY and 6% QoQ. Poonawalla Housing Finance Limited disbursement stood at Rs. 611 Crores, which is up by 57% YoY and 14% QoQ.

Let me now elaborate on our execution strategy during the quarter. Starting with business growth, we focused on developing diversified disbursement engine that has aided growth of organic disbursement. Organic disbursement rose 180% YoY, 32% QoQ. Over the course of last one year, our organic disbursements have increased 2.8x. We ended September at a monthly organic disbursement run rate of Rs. 1,300 Crores against given guidance of Rs. 1,000 Crores.

With the focus on the Direct Digital Program, the disbursement growth has been accompanied by lower customer acquisition costs compared to traditional distribution model and has also accelerated the customer acquisition. The DDP mix has risen to 47% in Q2 FY23 from 34% in Q1 FY23 and 17.5% in Q4 FY22, led by strong data analytics, cross-sell, upsell has also seen good traction contributing to overall growth and profitability early on. Our focus from day one has been on instilling the culture of building digital-first technology-led organization. I am happy to share that we have now fully operationalized in-house technology center dedicated to our digital, tech, analytics, and other agenda.

On liability side, despite the rising interest rate environment, our cost of borrowing increase was largely contained. As highlighted earlier, CARE upgraded our long-term rating to AAA/Stable and this would further help us contain the increase in cost of borrowing, despite rise of 190 bps in benchmark rate in this fiscal year so far and further rise. We are still carrying almost Rs. 1,300 Crores of our legacy borrowings at 9.5%. We recently started our capital market borrowing. We raised around Rs. 1,200 Crores in the last quarter via CP and NCD route. Otherwise, we are again amongst the lowest in terms of cost of funds if you do apple-to-apple comparison.

Having had a fantastic first half, let me take you through to what we can expect over the rest of financial year. While we are in a rising interest rate and liquidity-deficit environment, the market segment in which we operate, that is consumer largely and MSME, continue to grow. The ongoing technology disruption in lending, several digital-first, tech-led players like us, with the full-scale operationalization of our technology center, we will accelerate digital offering in our rapidly growing areas of embedded and contextual lending. In the upcoming quarter, you will see us leverage of our technology, digital, and customer service capability to further enhance our superior customer experience and thereby build a competitive moat. With a monthly organic disbursement run rate of Rs. 1,300 Crores in September 2022, we have a strong business momentum for the upcoming H2 FY2023.

We are confident that we will continue to have among the best asset quality in the NBFC space, and we will maintain net NPA less than 1% with our Management Vision 2025. Our current Opex to AUM stands at 5.9% since we continue to invest in capability building, technology, and invest in people. Also, we have given ESOP to more than 400 people, which is almost 35% covering manager and above level employees, and our total employee population of 3,200 on-roll people, it almost covers 15%, which is the highest in the industry. With this reduction of ESOP charge going forward, we expect a sequential decline in this ratio from next financial year onwards because there is Rs. 35-40 Crores ESOP charges since last 2 quarters, which will be there for the current year. But despite of that, there is an increase in the pre-operating profit. Also, there is a one-time cost and huge investment in the team as well as building digital and other capabilities. We are expecting drastic reduction in terms of Opex from next year onwards.

With the leadership team in place, best-in-class digital infra, and other technological capability, highest credit rating, expanding our production, and the best-in-class asset quality, we are confident of a strong growth trajectory in FY2023 and beyond, and now considering this exceptional performance, which is in line with our Management Vision 2025, I assure you that whatever guidance we have given, till date we have achieved, and we are going to achieve as per our stated vision.

Thank you everyone, and now we can start the Q&A session.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Sameer Bhise from JM Financial Institutional Securities. Please go head.

Sameer Bhise: Thank you for the opportunity and congratulations to Abhay and team for a superb quarter. I wanted to get a few data points before I ask other questions. Can you elaborate on the AUM mix on the focused business right now across products?

Abhay Bhutada: Thank you so much Sameer. Right now, we have more than Rs. 2,300 Crores in terms of pre-owned car. Auto lease, we have Rs. 286 Crores, and unsecured personal loan, business loan, loan to professional, we have Rs. 5,135 Crores. Then we have other products, which we acquired last year, the DA book, which is outstanding at Rs. 2,609 Crores, and the existing legacy book including few other products is around Rs. 1,540 Crores, and now we have housing Rs. 4,927 Crores and PHFL acquired DA Rs. 686 Crores, with total AUM of Rs. 18,560 Crores, and if you want to focus on a monthly number, then we have crossed Rs. 180 Crores on a monthly disbursement basis on our pre-owned car, then we are doing around Rs. 30 Crores per month on auto lease. We are doing almost Rs. 300 Crores on the business loan side. We are doing including digital ecosystem more than Rs. 250 Crores per month on the personal loan side. We are doing more than Rs. 130 Crores on the loan against property side. We are operating at 30 locations in loan against property. All other products, we are operating at 110-120 branches. So, I think this is one of the best numbers in the NBFC industry, because as of now, considering our monthly run rate of Rs. 1,300 Crores, we are just operating at 110-120 locations.

Sameer Bhise: Some details on the customers acquired maybe in terms of number of customers or profile will be helpful?

Abhay Bhutada: So more than 80% of our customers, they are 730-plus CIBIL, and this quarter, we have acquired closer to 4.65 lakh customers.

Sameer Bhise: Across all product lines?

Abhay Bhutada: Yes. Across all product lines this is the highest-ever customer acquisition, and now we are expecting this number will increase drastically over the period of next few quarters.

Sameer Bhise: Where does the written-off book stand at this point in time?

Abhay Bhutada: So, legacy write-off book, we have closer to Rs. 1,100 Crores. So, we have a write-off policy since acquisition of 90 days and 180 days. We have done a lot of write-offs against that as per the policy. So, we are at Rs. 1,100 Crores and considering the past recovery trend of 40-45%, and because of the early write-off, even you can consider 45% we are going to recover over a period of next 12 to 18 months.

Sameer Bhise: Okay I think for now this is helpful and probably get back in the queue for the questions if at all. Thank you so much and all the best.

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

Shreepal Doshi: Good evening and thank you for giving me the opportunity. The question was with respect to the discontinued book, you said it is close to Rs. 1,100 Crores. I suppose last quarter it was Rs. 2,000 Crores, and I think the coverage their last quarter was close to 9%. So, is there a write-off there or entirely it is broadly due to repayments? So, if you could just give some color on that.

Sanjay Miranka: Yes, there is a write-off. The total write-off is about Rs. 364 Crores, which we have done. Including policy write-off, it would be about Rs. 460 Crores. So, the discontinued book, has been written off. So, as we speak, the discontinued book has come down significantly to Rs. 1,540 Crores, which Abhay has talked about. But, if you take only the on-book, the discontinued book is down to about Rs 1,270 Crores.

Abhay Bhutada: So, if you remember, last quarter we have informed that we have created a management overlay of the one-time insurance stake sale profit, which we have utilized for the legacy book, which was created only for the legacy book. So right now, whatever on-book legacy book is there, except from the policy write-off, we are not expecting any additional write-off. However, we want to come out of this legacy book so that there will be a proper comparison, and by end of March, legacy book will be below Rs. 500 Crores of whatever will be there on-book.

Shreepal Doshi: The second question was with respect to the newer segments that we have entered in the last one year. So, while you did give some color that during the quarter, you have acquired 4.65

lakh customers with more than 730 CIBIL. If you could give some details on the bounce rates for these segments and one plus DPD number, so some of the asset quality indicators that you would be tracking, if you could give some color on that will be very helpful.

Abhay Bhutada: So, on that side, I think we are maintaining our 60-plus is less than 0.4%, and since we are the very few amongst the NBFC who do write-off at 90-plus unsecured and secured at 180 plus, so there is no major write-off in the newly acquired book. And considering our 18 months of experience in Poonawalla Fincorp, and the existing track record of Poonawalla Finance group NBFC, wherever 2-3 years tenure personal loan, professional loan, business loan, whatever experimentation was done, and there also we used to write-off at 90-plus. We carried the same overall learning, and right now, the 60-plus is less than 0.4%.

Shreepal Doshi: And Sir, what would be the bounce rate in some of the segments like MSME and personal loans?

Abhay Bhutada: So here in personal and professional loans, 30-plus is less than 0.10 because the segment which we are targeting; because of the low cost of fund and the digital acquisition, we are able to give a very fine rate as compared with any other larger NBFC, and I want to give you some additional data point here. Whatever initial assessment done by internal team members, I think we are getting first choice of rejection in terms of personal loan and the professional loan. The entire process is digital.

We have gone 100% digital across all our products, including pre-owned car. But in personal loan, professional loan, there is no DSA, so we are saving straightaway 3% to 3.5% the DSA acquisition cost. We have stopped DSA 4-5 months back, and this is completely direct and digital acquisition.

Shreepal Doshi: So, how much do we pay to the DSAs for these loans?

Abhay Bhutada: So personal loan, professional loan, there is no DSA. In case of business loan, we have some DSAs, and loan against property and pre-owned car, depends on the product to product and channel to channel.

Shreepal Doshi: So, what would be the payouts?

Abhay Bhutada: So, payout varies, but that is as per the industry standard.

Shreepal Doshi: So, if you could give some range, maybe say 25 to 75, or if you could give some range there.

Abhay Bhutada: So, for example, for business loan, we give payout anything between 2.5%-3.5% range, depend on the volume and slab. But there the IRR is 19%, we get upfront processing fees of

2% and additional other cross-sell income. In case of pre-owned car, again, we give around 2% to 2.5%, depending on the slab, and in case of loan against property, we give between 1% and 1.25%, depending on the slabs.

Shreepal Doshi: And in the housing business, so I read in the presentation that we have initiated the IPO, I suppose. So, what is the timeline and what is the thought process?

Abhay Bhutada: So as of now, we will not be able to give much detail. We have appointed the investment banker. The process is going on. Maybe in couple of months, in 2 to 3 months, we will be able to give you more detail on that. As of now, the process is going on as per the plan.

Shreepal Doshi: Got it Sir. Thank you so much if I have more questions I will come in the queue. Thank you and Happy Diwali to the entire team.

Moderator: Thank you. The next question is from the line of Harshvardhan Agrawal from IDFC Mutual Fund. Please go head.

Harshvardhan Agrawal: Sir, just wanted to understand the line item that we have this time, net gains from de-recognition of financial instruments, what does this pertains to?

Abhay Bhutada: So basically, as per our stated objective from the last quarter onwards, we have decided to come out of that existing Magma legacy book, and apart from the write-off, whatever was the zero DPD and because of that different customer segment in nature, we started selling that book as well.

Harshvardhan Agrawal: So, we have sold down some book and this is whatever the fee that we have got.

Abhay Bhutada: We got from the legacy sold out book, yes.

Harshvardhan Agrawal: So, this Rs. 33 Crores will recur every quarter or this is a one-time income.

Abhay Bhutada: This is a one-time income, and again, whatever is the additional recovery we will get, maybe in next 1 to 2 quarters, because as I have discussed just now, we want to keep legacy book to Rs. 500 Crores by end of March and may be by June 2023 we will be out of legacy book. So, one is a policy write-off or additional write-off, and second is we are selling because we are not able to do cross-sell on the existing Magma, agri, CV, CE, tractor kind of customer. So, we decided to sell that book, and now the balance legacy book will be less than Rs. 500 Crores, by March 2023.

Harshvardhan Agrawal: So, since because this is a one-off income, if I were to take off this income from our revenue line item and then see the quarterly growth between the AUM and the quarterly growth between our NII, seems like our NII was trailing the AUM growth. So how do I read it? Is it the incremental book coming at a lower yield, or the cost of fund is increasing at a rapid pace? How should one read into that?

Abhay Bhutada: Initially acquired book which was at a lower rate and now we have increased the rate from last 2 months. Initially we started to focus on a lower rate. But now we have enough scope, still we are offering the lowest rate as compared with any other larger NBFC. We have still scope to increase 100-150 basis points. So, we have increased 100 bps rate from last 2 months after the RBI rate hike, and now you will see further increase in the yield going further.

Harshvardhan Agrawal: Sure, and Sir, one last thing is about the credit cost line item. Due to the excess provision that we have done in the past, we are able to do some write backs over the last previous quarters. So how should one really build in the credit cost if you were to look at, say, FY2024 or even FY2025, just in terms of modeling the credit cost line item?

Abhay Bhutada: So basically, because of the write-off book still available, you will not see actual P&L charge on the same. But, however, credit cost, you can consider anything in the range of 0.5% to 0.7%.

Harshvardhan Agrawal: And how long we will have this flexibility of write backs on credit cost?

Abhay Bhutada: Though we have done early write-offs from the legacy book, but we need to recover that, right, and we are going to recover almost 45-50% of that. So that will take 12 to 18 months. So that is additional cushion available against the balance legacy book available. So that is why we are not expecting any losses from the balance legacy book. In fact, we may expect write back of Rs. 150-200 Crores over a period of next 12 to 18 months.

Harshvardhan Agrawal: Right. So, sir, just to understand that, is it for next 4 quarters, we may still continue with some of this negative credit cost line item, for fair assumption to make?

Abhay Bhutada: Yes, at least for next 2 to 3 quarters.

Harshvardhan Agrawal: Sure, thanks a lot Sir. I will get back in the queue for more questions.

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

Kaitav Shah: Good evening, Sir. Congratulations for good set of numbers. My question is more related to your customer acquisition. If you can give us more detailed understanding about how much is new to bank, how much is customer profile in terms of own organic sourcing and how much is DSA acquired, if you can break it up along those lines?

Abhay Bhutada: So, basically, if you see out of our acquired total customer base, so our Direct Digital Program is running well. We have crossed 47% for the total disbursement, and more than 95% is directly acquired customer under Direct Digital Program with our digital ecosystem partners, and only 5% of the total customer count is via DSA route. And here more than 95% are credit-tested customers, GST tested customer, and hardly there are less than 5% new-to-credit customer that too under partner ecosystem wherein we have done 2 or 3 co-lending wherein we are getting 10% FLDG. So, there is no actual loss to us.

Kaitav Shah: Fair enough I think that was my broad question. Thank you.

Moderator: Thank you. The next question is from the line of Hena Vora from Systematix. Please go ahead.

Hena Vora: Good evening. Can, I just know the AUM mix. I missed up your numbers.

Abhay Bhutada: You are talking about secured or unsecured AUM mix?

Hena Vora: No, the focused business AUM mix.

Abhay Bhutada: Product-wise, we have already stated, but I will just give you an idea. Housing, we have Rs. 5,612 Crores, and Poonawalla Fincorp at standalone, we have more than Rs. 13,000 Crores. Out of that, professional loan, personal loan, business loan, and other digital unsecured products, we have Rs. 5,135 Crores, loan against property Rs. 1,241 Crores, then existing acquired DA Rs. 2,609 Crores, our existing legacy book Rs. 1,540 Crores, auto lease around Rs. 286 Crores, and pre-owned car, which is Rs. 2,317 Crores, and on a monthly basis, we are doing Rs. 180-185 Crores on pre-owned car, auto lease around Rs. 30 Crores, business loans Rs. 300 Crores, personal loan around Rs. 250 Crores, loan against property around Rs. 130 Crores. Housing side, we are doing around closer to approximately Rs. 200 Crores per month.

Hena Vora: Okay thank you. That was my question. Thank you.

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

Kunal Shah: Hi, so firstly, sorry, with respect to this Rs. 33 Crores, and overall. when we look at it in terms of the provisioning write back of almost Rs. 41 odd Crores. So cumulatively, maybe from the written-off book, would it be fair to assume that maybe on a net basis, the recoveries are more than Rs. 70 odd Crores? I did not get the difference in terms of the provisioning write back and what is there in fair value.

Abhay Bhutada: So, Kunal, recovery from the write-off book for the quarter was Rs. 75 Crores.

Kunal Shah: Yes, it was Rs. 75 Crores. Okay, perfect. Got it, and when we look at it overall, in terms of, say, Stage 1 and Stage 2 PCR, which is also coming off on a QoQ basis, particularly on the PFL side, so this is largely because maybe there was some write-off book out there also or maybe something which was written off from that pool as well, which is leading to this kind of a decline in PCR?

Abhay Bhutada: Yes. So basically, we do write-off of unsecured at 90-plus and again secured at 180-plus for legacy book as well as for the new book, and considering the last 18 months' performance, there are no early delinquencies also in the new book. However, yes, because of the write-off of the legacy book, it will get reduced going further, because we require Stage 3 provisioning only and only for the secured book.

Kunal Shah: Got it, and on the restructured side, so out of Rs. 467 crores, Rs. 211 Crores is zero bucket and the balance also we are quite comfortable because I think it is slowly coming up, but entire thing is not yet out maybe out of the moratorium. So maybe any expectations on maybe the slippage from that pool or that is performing well?

Abhay Bhutada: So that book is performing well. As we discussed, out of this Rs. 467 Crores, now Rs. 211 Crores, which is into zero book, almost 45% of the restructured book, and against the pending restructured book, again, we are getting EMI, and whatever we wanted to write-off, we have done the write-off in the last 2-3 quarters from that pool as well, because this is 100% legacy book.

Kunal Shah: Okay. So there also the write-off is done. So, there should not be any further provisioning coming in from the restructured side?

Abhay Bhutada: Yes. Because if you see, Kunal, this GS3 number also, we have aligned to new RBI norm. That is why our GS3 and NS3 numbers have reduced drastically, but at the same time, if you look our GS3 and NS3 numbers that is much lesser as compared with the GNPA and NNPA numbers.

Kunal Shah: Sure and given now maybe the experience over the past few quarters, the run rate which you have highlighted on a monthly basis with respect to, say, BL, PL, LAP as well as maybe on the pre-owned side. Do we see that maybe either of these segments would do relatively better because we have still been, say, on an investment phase and that is yet to scale up? No doubt, there will be overall business growth, but in terms of the proportion wherein they are, do we see couple of them significantly outperforming the other?

Abhay Bhutada: I think at overall consolidated level, we are maintaining 70:30 secured and unsecured mix. However, if you see whatever product we launch, pre-owned car, business loan, personal loan, professional loan, and loan against property, as I told you, we are operating at only 30 locations in loan against property and all other products at 100+ locations. So, if you do peer-to-peer comparison, then I think we are in the top 2 or top 3 in most of the products, and this is just a start. Now we have completed the whole consolidation phase. Now since last 2 quarters we are in growth phase. So, the closing run rate will be much, much better as compared with our first half. Second half will be much better, and the actual growth is also more. Because of this legacy book write-off, on paper QoQ, the overall AUM growth looks on a lesser side. But because of the legacy book write-off and discontinued book run down so fast, the actual AUM growth is much more in all the newly launched products, and the segment which we are targeting, we are not expecting any early delinquency or credit cost, whatever, we have given the guidance of 0.7% to 0.9%, I think we will be able to maintain that.

Abhay Bhutada: And Kunal, as we discussed in the last quarter also, that Opex will get reduced drastically in the next year. See, we have covered almost 430-450 people in ESOP and the RSO. So that is a notional charge on the P&L. So last quarter, it was almost approximate Rs. 40 Crores. This quarter also is Rs. 44 Crores. If you see our pre-operating profit, it would have been higher by almost Rs. 40-45 Crores so actual profitability is much, much higher. But despite of that, yes, there is an increase in the pre-operating profit and across all other parameters.

Kunal Shah: Yes. So, this Rs. 160-180 Crores would be there for this fiscal and then maybe next year onwards this should run down.

Abhay Bhutada: Next year, it will get reduced to maybe around Rs. 55-60 Crores, and third year it will be around Rs. 20-30 Crores because in the first year itself to retain the top talent, we have covered the larger population till the junior level.

Kunal Shah: Okay. So Rs. 160-180 Crores in this fiscal and coming down to Rs. 55-60 Crores next year, and then Rs. 20-30 Crores in a year after that in terms of the cost.

Abhay Bhutada: Yes. There are a lot of one-time costs as well, since we are largely investing in technology and team we are building, so there are a lot of onetime costs in the last 2 quarters or maybe next 1- 2 quarters, but that also will get reduced in the next financial year.

Kunal Shah: Got it. Thanks. All the best and wish you a very Happy Diwali to you and your entire team.

Moderator: Thank you. The next question is from the line Dhaval Gala from Aditya Birla Sun Life Asset Management. Please go ahead.

Dhaval Gala: Good evening and Congratulations on good set of numbers. Few questions. First being, Abhay, if you could articulate around AUM growth, and basically, we do understand right now we were in restructuring or a reorganizing phase because you were running down some book, which you did not want to grow, and you were growing personal loans and other segments. If you could talk about is how do one look at sustainable growth. Also, basically, if you could provide some more color on customer profile also and how sustainable the growth would be in the medium-term.

Abhay Bhutada: So, in terms of growth if you see September 2021, the focused AUM was Rs. 10,900 Crores. Now within one year, we have reached Rs. 17,000 Crores in terms of our focused growth and discontinued book at Rs. 1,545 Crores, the total comes to Rs. 18,560 Crores. I think almost more than 80% growth in terms of the focused AUM growth in one year, but as per our Management Vision, 3x AUM of March 2021 to March 2025, we will be able to grow considering the current monthly run rate, considering the capability we have, considering the market opportunity available, we will be able to grow anything between 30-35% over a period of next 3 years to achieve our 3x growth by March 2025. And on the customer profile side, I think mostly we are targeting the bureau-tested customer. Data, technology, and the overall tech center is more than 200-plus team now. GST tested customer, TDS tested, so, a lot of informal income segment wherein people are paying statutory dues on time, PDF banking is available. Almost everyone is focusing on the same. But at the same time, in terms of TAT, in terms of customer service, in terms of product proposition, I think we are far better as compared with other large competitors. Basically, what feedback we got from lot of customers that we are the only NBFC at a larger scale who is offering zero prepayment charges across all our products if they pay from the own funds. At the same time, of course, we will charge some penalty if there is a balance transfer. But in terms of product proposition, no hidden charges, low rate, processing fees, TAT, overall customer product proposition, and the digital user experience, so customers are giving clearly first choice of rejection in most of the products, and of course, the Poonawalla brand is there as a trust factor.

Dhaval Gala: Just a couple of more questions. One on the customer franchise, if one has to understand, I do understand your articulation around new segments of growth. But what is cost of acquisition in the real sense, and when you mentioned about operating leverage, a couple of questions back somebody asked, how do one consider what type of customer base you are building, and do you have any analysis that how much of cross-sell you will be able to do over a period of time, long term, and therefore, operating leverage can come down? This can come down and you can have higher operating leverage.

Abhay Bhutada: So out of our total monthly disbursement, total 47% is our DDP, which is direct digital ecosystem, wherein our total customer acquisition cost is less than 1%, and in case of the other DSA cost and a few other costs, the customer acquisition goes to around 1.5-2% on an average basis, and in terms of cross-sell, I think whatever data analytics we have done, we will be able to do a lot of cross-sell. Already we have started cross-sell. We will start giving numbers in a quarter or two. But on a steady state basis, one year down the line, I think we will be able to cross 30-40% of the existing database in terms of cross-sell. Now, we are launching the EMI card, credit card or the consumer loan, because we keep getting inquiries on the call center from the customers that they are looking for most of the services from the Poonawalla, reason being the existing customer. So, I think whatever early signals we have, you can expect, we will focus on loyal customer base, and the reason I told you just now and to Kunal also, about the trust and first choice of rejection we are getting because of the no hidden charges and product proposition what we have.

Dhaval Gala: Right now, I understand when everyone is very improved asset quality coming from a higher base of COVID, and even for us, we were also in a process of merger and therefore, we had done a lot of high provisions last year. Now if you could talk about what is the likelihood of sustainable credit cost for our company, and when you build different products, what type of credit cost you build or estimate when you underwrite? So, it means if you could talk more about underwriting skills and also what type of asset quality and credit cost would be sustainable?

Abhay Bhutada: Basically, the segment which we are targeting, whatever analytics we have done on the existing customer and the proposed customer base, next year you can consider the credit cost around 0.5%. But on a steady-state basis range, I can give you anything between 0.5-0.8%. We are doing write-off at 90-plus, so we have to control the credit cost at the time of on-boarding itself because we have not changed policy. It is not only we are following only for the legacy unsecured book or legacy secured. This policy we have decided in March 2021 at the time of acquisition for both secured and unsecured. So, we do all the secured product write-off at 180-plus and unsecured at 90-plus. So, to control the credit cost, we follow the first-time collection and 30-plus dpd as our main trigger.

Dhaval Gala: And your management overlay provisions, when does that get kicked in? When do you use them, any policy around that, and how long do you continue to provide, mean, what type of proportion you want to create?

Abhay Bhutada: Basically, we have created this buffer only on the legacy book. We have not utilized any of the management overlay towards the new book. New book is performing quite well, better than our expectation, and this management overlay, I think now, as I told you, by end of March will be less than Rs. 500 Crores. We have started either selling the legacy book or writing off the legacy book, and still, we are carrying Rs. 1,100 Crores because of the total write-off book, and out of that, we will recover Rs. 450-500 Crores. So, you can expect there will not be any additional management overlay we will create going further for the legacy book because we can expect write-back, but not losses out of the legacy book.

Dhaval Gala: And basically, the entire management overlay would be used for the legacy book?

Abhay Bhutada: Yes, that is created only for that purpose. We have not utilized any of the management overlay for the new book. It is only for the legacy book.

Dhaval Gala: And when does, according to you, our legacy book basically runs down to zero?

Abhay Bhutada: June 2023.

Dhaval Gala: Okay. So, by then whatever is not required to provide, you could write back in the ensuing quarter, or you will choose to keep the buffer as it is?

Abhay Bhutada: Yes. I think we cannot use that buffer. We will have to write back whatever with the balance provision as per the law and as per the rule as well, and whatever the write-off book is there, that Rs. 1,000 Crores, that, of course, we can utilize towards the legacy book, and as and when required, like for example, we have recovered Rs. 75 Crores last quarter. So, over a period of maybe 18 months, you can expect the quarterly write-back from that book.

Dhaval Gala: Okay. Abhay, last question on the treasury side if you could talk about our cost of funds and also if you could talk about what is incremental cost of funds and what according to you would be basically the benefit because of upgrade in the rating profile and the name Poonawalla, what type of repricing is already done and whether our cost of funds are now on a like-to-like basis to our rating or there is room to improve more?

Abhay Bhutada: Yes. So right now, cost of fund is at around 7.12%, and we can expect 20 bps or maybe 40 bps, depending on the RBI, QoQ basis, you can expect that hike. However, we just started capital market borrowing, and there is a scope to borrow more via CP route as well as we are carrying Rs. 1,300 Crores of legacy book at 9.5%, which will get close over a period of next 11-12 months. So, considering that, I think the effect will be very gradual, and we have started increasing the rates since the last 2-3 months. So, I think we will not face any issue due to the cost, already we are amongst the lowest in terms of cost of borrowing. And if you see recent, all our PSU bank sanction, first time we have received almost 7-year money at around 7.25% rate, and now we will have to see any further increase from these banks. But again, in all the AAA-rated NBFC, around 5-6 AAA-rated NBFCs, we are amongst the lowest in terms of, if you talk about, the bank borrowing. So now with the increase of CARE AAA rating, you can expect 20-25 bps additional benefit via capital market borrowing as well as 10-15 bps more benefit in terms of bank borrowing.

Dhaval Gala: Thank you Abhay thanks a lot for patient answering.

Moderator: Thank you. The next question is from the line of Sameer Bhise from JM Financial Institutional Securities. Please go ahead.

Sameer Bhise: Thanks for the follow-up opportunity. So, the discontinued book has reduced by Rs. 760 Crores or Rs. 740 Crores on a sequential basis. Can you just give a split between how much was sold down? How much has been a normal repayment?

Abhay Bhutada: Rs. 330 Crores we have done a write-off, Rs. 226 Crores we have sold to one of the private banks and remaining was a policy write-off of only legacy book. So, this is the breakup.

Sameer Bhise: What was the interest reversal for the quarter?

Abhay Bhutada: It was around Rs. 5 Crores.

Sameer Bhise: Okay. Sure, and just coming back to the Opex part, just wanted to get a sense on how the number of employees is shaping up, given the large collection team you had inherited at Magma and how things are moving there with respect to a number of employees?

Abhay Bhutada: We have around 3,200 on-roll people and around more than 2,000 people off-roll basis. So, as we speak, we have 5,200 people, and out of that, we have more than 50% on the collection side, and this is the best part, that was the main reason behind Magma acquisition because we wanted to start with our experience of Poonawalla Finance, now in Poonawalla Fincorp, consumer loan and a lot of other products, wherein you require some kind of collection. So, now we have good enough strong collection infrastructure available and on-roll as well as the off-roll. As we move forward, we have done a lot of reskilling and retraining. Out of that, lot of people are willing to move to the sales also, and remaining, we will continue in the collection side. On the legacy on-book of Rs. 1,300 Crores and the write-off book of Rs. 1,100 Crores, so almost still we are carrying more than Rs. 2,300 Crores of legacy book, including write-off. So, for that, we need the collection infrastructure, which we have because in the existing Magma legacy book, maximum 50-60% is the cash collection. Right now, in the new book, there is no single cash collection and 100% on-boarding via digital route, and 100% NACH mandate, 100% digital disbursement, and 100% digital collection. So here, the 60-plus itself is less than 0.5%, and we are not expecting more than 0.9% credit cost. So, we will not require much of the field collection. But at the same time, now we are moving towards a high-yield product, small personal loan, consumer loan, EMI card, co-brand credit card. Over a period of next 3 to 4 quarters, we are going to launch a few high-yield products, and again, until that time, next 12 months, when they will complete all the legacy book collection, they will be all useful because we have done the fresh assessment, and this is all desired population. Already there was much more attrition, and we have allowed them to go because they wanted to focus on CV, CE, tractor as per their interest area. So now already headcount got reduced by more than 1,500-2,000, which you will see a good amount of Opex reduction in that as well in the coming quarters.

Sameer Bhise: Thank you Sir. That is all from my side. All the best.

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

Shreepal Doshi: Sir, thank you for giving me an opportunity once again. Just on the DSA sourcing front, I wanted to understand what is the responsibility, as in like is it only with respect to lead generation or they are also responsible for some other, say, documentation and verification aspect also. So that is the first question. The second question is if you could give us the pricing range for our non-digital products, that is, pre-owned cars, machinery loans, auto lease loans, and what would we be paying to these DSAs for these products?

Abhay Bhutada: So if you see the IRR, I think on the business loan side, we are maintaining an IRR of around 18.5%, pre-owned car around 15.7%, loan to professional and personal loans we are able to match average rate of 13.5%, the segment which we are targeting, and coming back to your DSA question, their responsibility is to just login the file as per the requirements. Since our entire process is digital, we have given them all the apps and whatever required login process, we have given them enough training, and now they are only logging the file. Wherever required, our field sales people and wherever we have the branches, they help them with training as well as in terms of login. Going further, our focus is more and more on the digital. If you see, we just started pilot in Q4 of last financial year, and in the last quarter itself of the last financial year, we did almost 17.5% of our direct digital ecosystem, which almost increased double to 34% in quarter one, and now in Q2, it is almost at 47%. So going further, you will see more and more focus on the direct and the digital rather than the DSA.

Abhay Bhutada: If you see loan against property, pre-owned car, or business loan this is the industry practice, I think this is largely driven by the DSA. But yes, our focus will be more and more on the digital.

Shreepal Doshi: Got it, and currently, in my earlier question, you had said that you paid 2-2.5% as a payout to these DSAs, right?

Abhay Bhutada: Yes, in case of business loans.

Shreepal Doshi: Right. Got it. Thank you so much Sir.

Moderator: Thank you. The next question is from the line of Sagar Jethwani from PhillipCapital. Please go ahead.

Sagar Jethwani: Sir, I missed it, sorry. You mentioned that you will see a lower Opex next year, and what is the reason for that? I missed it completely.

Abhay Bhutada: Very good question. See, basically, one, we are investing largely on the technology side in the current year, we are investing largely on the team as well, strengthening the leadership team, and most important, we wanted to retain the people. We wanted to focus more on the ESOP till our lower-level management. So out of my 3,200 on-roll employees, we have covered almost 450 people via terms of ESOP, and we have 1,000 people, manager and above, wherein this count comes to 45%, which is the highest in India. So, from that perspective, the current year, the ESOP charge itself is Rs. 40 Crores per quarter, it is almost Rs. 160 Crores in the current year, which will get reduced to Rs. 50-60 Crores in the next year, and again, it will get reduced further. This is, again, a notional charge on the P&L. But despite of that, if you see, there is a YoY and the QoQ increase in the pre-operating profit, there is an increase in the revenue, and this one-time cost of technology, team, and ESOP will get reduced drastically from the next year, so you can expect a 1-1.5% reduction in terms of Opex to AUM from next year onwards. But on a steady state basis, 2 years down the line, I think we will be able to maintain a level of, I can give you the range 3-3.5%, 2 years down the line.

Sagar Jethwani: Okay, and what is the mix between secured, unsecured, and also between urban, semi-urban, and rural loan book?

Abhay Bhutada: I think we are focusing on urban and semi-urban. I think more than 60-70% is urban and remaining is semi-urban. In terms of secured and unsecured, as on 30th September, 72% of AUM mix is secured and 28% is unsecured.

Sagar Jethwani: And also, we are on track to achieve Rs. 21,000 Crores of AUM guided, and by FY2025, the plan is to get there to Rs. 40,000– 45,000 Crores of AUM. How can we see FY2024, I know it is a little bit early to ask, but still, if you have any target in mind maybe.

Abhay Bhutada: You can assume from here on, the QoQ growth, anything between 6-8%. On a YoY basis, next 3 years, you will see growth in the range of 30-35%. Basically, I just want to add here, we have a capacity to disburse Rs. 3,000 Crores per month. We have not fully utilized our capacity. We have just crossed a monthly run rate of almost Rs. 1,300 Crores from September 2022. On the basis of the last 6 months track and the basis of last 6-9 months consistency in terms of organic number, we are pretty confident of H2 and beyond as well.

Sagar Jethwani: That is very helpful. Thank you, Sir.

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

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. Thank you.

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