



“Equitas Small Finance Bank Limited
Q3 FY '25 Earnings Conference Call”

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Moderator:

Ladies and gentlemen, good evening, and welcome to the earnings call of Equitas Small Finance Bank Limited's financial performance for Q3 FY '25. We have with us today Mr. P. N. Vasudevan, MD and CEO; Mr. Sridharan N, CFO; Mr. Murali Vaidyanathan, Senior President and Country Head, Branch Banking, Liabilities, Product and Wealth; Mr. Rohit Phadke, Senior President and Head, Assets; Mr. Natarajan M, President and Head, Treasury; Mr. Dheeraj Mohan, Head, Strategy.

As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing star, then zero on your touch-tone telephone. Please note that this conference is being recorded.

I would now like to hand the conference over to Mr. P. N. Vasudevan. Thank you, and over to you, sir.

P. N. Vasudevan:

Thank you. Good evening to all of you, and thank you for dialling into this call. I would like to talk about two items, post which Dheeraj, our Investor Relations and Strategy Head, would talk about the rest of the business. I would like to talk about the stress in the MFI sector, which is an immediate focus to start with and after that, I would like to touch upon the fundamental strategic platform that we have been building for the bank from a medium- to long-term perspective.

Microfinance portfolio was behaving normally till March '24. During Q1 of this year, for the first time in Equitas, we saw the X-Bucket collection efficiency slip marginally from the normal levels of about 99.4% to about 98.9%. However, it was believed that this was due to the combined effect of heatwave and the General Elections in April, May of '24.

And so the industry and us included were quite caught by surprise when the collection efficiency dipped further in Q2 for no apparent external reasons. In our case, it dropped from 98.9% of Q1 down to 98.2% in Q2. And when this happened across geographies, it was clear that an important reason for the stress was as much internal as external.

Around 10% to 15% of customers availing loan from more than 3 lenders and even going up to 5, 6 lenders were common earlier also. While this caused some level of stress, it was still very much within tolerable limits, as there was an MFIN norm that all lenders put together, the loan cannot exceed INR1.25 lakhs.

However, this cap was removed effective Jan '23 for reasons that we all know. And it was not replaced by a norm but a general amorphous cap of something in the range of around INR2.25 lakhs kind of backwards from the prior norms.

Somewhere during the calendar year 2023, because of this change, the actual amounts borrowed by the customers had gone up probably at a pace which was too rapid. And this was reflected in the strong growth in the industry during that point in time.

But while we know all of this, and we have an idea of the players and the amounts involved, I believe that what is not really understood or clear is also there's some kind of a parallel lending happening to the same set of borrowers by so called app loan companies.

When I visited some of the customers to understand the level of leverage, I often saw that they had taken many small loans from app-based lenders. These loans were typically small in the range of INR5,000 to INR25,000 yet with short repayment tenures, the monthly EMI does work out to some decent size.

And probably, this is adding further to the kind of stress that the customers are facing in terms of our leveraging. So we may have to see how at the industry level we get all lenders to the segment to somehow fall in line with the MFIN guardrails 2.0 that's been rolled out effective Jan of this year.

In our portfolio, we have seen that X bucket efficiencies stabilized in Q3. But this is not really enough. We have put in many initiatives and hope to see an improvement in the same over this and next quarter. Because of a 6-month lag between X bucket slippage and eventual credit costs, we should see elevated credit cost in MFI for this and next quarter also arising out of slippages in the second and third quarter of this year depending on improvements in the X-Bucket efficiency we might see in Q4. Based on that, we should be able to predict some level of moderation in credit cost hopefully from Q2 or Q3 of the next financial year. Of course, as we speak, we are also aware of certain recent developments in Karnataka. So the outcome of that anyway needs to be addressed as the picture unfolds there.

In terms of diversification, in Equitas, we started the journey of diversifying from 100% Microfinance book to other forms of lending, secured forms of lending, way back in 2011. Presently, we have about 14% of our portfolio in Microfinance and the rest being secured. We will continue on this path and expect to see the share of Microfinance going down into single-digit shortly.

Micro Loan Against Property or MLAP is a product which we had introduced again way back in 2012, '13. This is basically for funding small businesses from INR2 lakh to INR7.5 lakh secured against house property. We have completed two cycles of this product with is typically a 5-year loan product. Out of about 2.3 lakh customers we have financed MLAP over the years, we have had to take legal recourse to repossess the property only in about 690 cases. And out of this, we actually had to sell the house only in 23 cases while the rest have either settled by the customer themselves or is work in progress. This shows our ability to underwrite properly and determine the right amount of loans that these customers would be able to borrow and repay.

The MLAP product addresses typically the 15% of the top end of the MFI customer segment. We have rolled out special emphasis on this product during this year, resulting in the disbursement in MLAP doubling during the year. Further emphasis is being given with an objective of trying to replace as much as possible the rundown in the MFI books by the MLAP book.

Now I come to the second part of what I wanted to cover which is the medium- to long-term strategic positioning of the bank. Our objective has been to build a stable, sustainable and scalable business model over the years. As per this on the lending side, we have now built a secured book of over 86% of the portfolio, comprising of Small Business Loans, Affordable Housing, used vehicles and MSE finance for working capital.

All these businesses have large unmet credit demand and address the requirement from the informal sector borrowers. Banks, by and large, have been absent from this market for all these years and given our strength built over the years, we do have a very strong competitive edge in the space. These products have been credit tested over the past decade through multiple headwinds such as GDP slowdown, demonetization, corona, etcetera. Through all those headwinds, the credit costs for all the rest of the products have remained within a very accessible narrow range.

Affordable housing finance, which is also having a comfortable GNPA and credit cost, has yet to breakeven being a new product but contributes 12% to the portfolio. This is expected to turn black next year which should hopefully help improve the overall profitability of the bank.

We have launched, as I mentioned earlier, liability strategy 2.0 during the current year. The objective is to improve stickiness of depositors, which will in turn enable us to reduce the interest rates that we offer and reduce the differential between us and the large banks in terms of interest rates over a period of 3 to 5 years.

On the liability side, most of the standard offerings are already in place, such as investment options, trading, ASBA and bill payments. On the asset side, affordable housing, used cars were the only ones that we could offer till now. This quarter, we have rolled out personal loans for deposit customers and credit cards for deposit customers will go live by March.

Based on the level of product consumption by depositors, we will take calls on reducing our interest rates on deposits. During this year, we have changed twice the interest rates on certain slabs of savings accounts, yielding a reduction of about 13 basis points in savings account interest cost.

We also reduced our peak TD interest rate during Q3 by 25 basis points. For the next 3 to 5 years, as we reduce our cost of funds, we should be able to further improve the quality of our borrowers. And given the large unmet credit demand from this customer segment, we should be able to sustain healthy growth with quality.

To sum up, the bank is going through the short-term impact of the stress in its Microfinance portfolio. However, the platform on which the bank has been built remains robust and strong and we should be able to sustainably and profitably grow this over the next few years.

I'll now hand over to Dheeraj for taking us through other business numbers.

Dheeraj Mohan:

Thank you, Vasu. Good evening to all of you. As you all know, Equitas operates at the grassroots of the economy and predominantly deals with the informal workforce on the lending side, while seeking deposits from the mass and mass affluent segments.

In our limited perspective, we are seeing a marginal uptick in economic activity, continued tightness in liquidity, limited growth in household incomes, and robust credit inquiries across segments and overall tightening of credit norms. At Equitas, we operate across eight lines of business, which are our liability franchise, the treasury business, which we set up in 2016, Small Business Loans, Vehicle Financing, Microfinance and micro loans, Affordable Housing, MSE finance and NBFC finance.

Our deposit franchise currently stand just north of INR40,000 crores and registered a healthy growth of 26% backed by strong growth in retail term deposits of 31% in a challenging environment. Our CASA remained stable at 29%, and we saw some uptick in current account balances.

However, growing SA or savings account balances continues to be a challenge as depositors prefer parking money in term deposits given the uncertainty of when the interest rate cycle may turn. Our total retail deposits, that is retail TD and CASA stands very healthily at 73% to the overall deposits. Our LCR stands at 184.8% and CD ratio comfortably at 88.6% as of December 2024.

The NRI business continues to attract depositors and is laying the foundation for the soon to be launched AD-1 business. The wealth and third-party distribution business is also moving along well. Today, we process around 33,000 SIPs and has handled a volume of close to INR20,000 crores in ASBA during this year.

Three quarters back, and this is also what Vasu had mentioned in his opening commentary, we had spoken about liability 2.0 strategy. The strategy is focused on two aspects to give Equitas a strong competitive edge in the long term.

Firstly, we aim to bring our cost of mobilizing deposits down through operational efficiency and improved productivity. And secondly, to narrow the cost of funds gap between Equitas and large universal banks and also get it a notch lower than the AAA-rated NBFCs.

To achieve this, it was critical that the bank develop a wide range of products and services to cross-sell and create stickiness among depositors as well as leverage technology to improve customer experience and service. Over the past few quarters, we are focused on putting this in place.

With the launch of credit card, personal loan and soon to be launching AD-1 services, along with products like car loans, housing finance, services like digital focus, wealth management, ASBA, etcetera, for savings account holders, we now have a strong proposition to build a loyal and sticky customer base. We are hoping all of this will help us in our liability 2.0 strategy mentioned earlier.

These initiatives have also given us room to revise our SA rates and drop our peak FD rates by 25 basis points. However, we are being very watchful and cautious given the current liquidity scenario. The rate revision has translated into a drop in the cost of SA by 13 basis points, and our FD cost should see some moderation in the coming quarters. This has helped keep our cost of funds stable at 7.49% despite raising INR500 crores in Tier 2 bonds during the quarter.

As the deposit franchise matures and we acquire good quality depositors, the focus is now on leveraging our customer base for cross-sell opportunities. Work is going on to strengthen this with data analytics through propensity models, digital marketing and active customer engagement.

On the technology front, we have had a few important rollouts. Our new scalable state-of-the-art CRM has gone live across branches. This is helping us service customers digitally, leverage biometrics for instant paperless servicing and track customer journeys from lead to conversion to servicing. Our proprietary cloud-based loan origination platform for personal loans and credit cards is live and will aid in cross-selling initiatives too.

The much-awaited revamped mobile banking application is being rolled out to customers as we speak, and initial feedback has been very encouraging. We hope all of you who have accounts with us give it a try and share feedback with us. We will now embark on creating a super app platform that will significantly enhance experience depositors will have with the bank.

On the treasury business, we made INR39 crores from profit on sale of investment, and the team now manages a book of INR9,500 crores. Our SLR book stands at INR8,300 crores as on end of December.

Moving to other lines of business on the asset side. Our advances has been -- our advances growth has been soft with a growth of 14% year-on-year as Microfinance continues to degrow. Our secured book or non-MFI book grew 20% year-on-year led by robust growth in -- of 27% in Small Business Loans.

The bank continues its strategy to focus on higher-yielding products like Micro LAP, used commercial vehicle loans and car loans. As a result, gross yields on advances inched up 6 basis points quarter-on-quarter despite a slowdown in Microfinance.

I will take a few minutes to give you a quick update of some of the major segments. Small Business Loans, the bank's flagship project, which started over 12 years back, continues to grow well, clocking a 27% growth in advances year-on-year. With an average ticket size of about INR7 lakh and a semi-urban focus, it is the most profitable book of the bank.

The GNPA continues to hold well at 2.34%, and we see no signs of contagion for Microfinance spilling over. The business operates from over 200 branches across 12 states and the bank plans to expand its network in Andhra, Telangana, Karnataka in the coming year. We have provided more granular deposits in our PPT too.

Coming to Vehicle Finance, the overall growth has been slow at 14% as we continue to defocus on new commercial vehicle loans, as we anticipated a negative market cycle to play out in the SCV segment. However, our UCV book has grown steadily at 19% and used car loans clocked a strong healthy growth of 55%. Our overall loan book is now INR1,700 crores for cars.

Our VF business operates out of 260-odd branches and continues to enjoy a long runway for growth given the level of under-penetration. The book is largely small and light commercial vehicle focused and targeting FTU and FTB segments. We are now seeing growth to come in the used heavy commercial vehicle segment in the coming quarters.

Our Affordable Housing book now is INR4,500 crores, and we continue to invest in broadening its network by leveraging our existing branches. With an average ticket size of INR12 lakhs and an NPA of 1.36%, this book remains healthy and has also seen improvements in yield during the year. We are now focusing on improving profitability of this book as the business matures.

Other products like MSE and NBFC plans continue to remain small, and the business growth is determined by how the interest rate cycle plays out in the coming months. On overall asset quality parameters, we have seen a good improvement in net slippage as it trends downward from Q2.

Net slippage for Q3 is 3.15% compared to 3.31% in the previous quarter. Improvement came in as net slippage in the Microfinance book improved considerably from 2.28% in Q2 to 1.11% in Q3. However, MFI continue to deteriorate as net slippage climbed sharply from 8.31% to 14.16% in Q3.

The 1 to 90 DPD at the bank level also improved 47 basis points as additional initiatives were taken to improve collections in MFI. We also added close to about 1,000 employees largely in MFI during the quarter.

Coming to the overall financial performance of the bank in Q3. The balance sheet has grown 22% year-on-year and is now above the INR50,000 crore mark. Margins remained under pressure at 7.39%, a decline of 33 basis points, mainly due to the drop in the MFI business mix and drop in treasury yields.

Credit costs came in at 2.65% as we utilized INR38 crores from the INR100 crores stressful provision created in the previous quarter. GNPA closed at 2.97% and NNPA at 0.96% as we focus on getting the bank in line with the universal banking guidelines for SMEs. Lastly, the bank registered a PAT of INR66 crores with an ROA of 0.53% and an ROE of 4.44%.

I thank you all for patiently listening to me. Now we'll -- the operator can open the call for questions.

Moderator:

Our first question comes from Rajiv Mehta from Yes Securities.

- Rajiv Mehta:** Just a question on the X bucket collection efficiency. If you can share the latest numbers across products within Vehicle Finance, SBL and MFI. And whether have you seen further improvement in January versus December?
- P. N. Vasudevan:** X bucket, as I mentioned here in the opening remarks, was 98.2% for the third quarter and it was at a similar level in the second quarter, while it was 98.8% or 98.9% in the first quarter.
- Rajiv Mehta:** Yes, sir. But this is MFI loan, right?
- P. N. Vasudevan:** That's right. It's for the MFI.
- Rajiv Mehta:** Correct. And other products?
- P. N. Vasudevan:** Other product, X bucket, I mean -- and that's -- I don't know whether that's relevant because I don't even have that data immediately. Yes, but typically, the MFI is very critical to measure X bucket because the percentage of collections that we do out of X bucket flow in Microfinance is much lower.
- In other products because generally the collection efficiencies are much higher in the OD bucket. And so the eventual flow into NPA is not that much. So X bucket is an important parameter that's measured internally but we don't share it with investors. Sorry.
- We have given that. Okay, sorry. It's there in page -- okay, okay. Yes, that's right. So we do have this data from our internal review processes, but it's not that relevant, so we don't share it with the market. Microfinance we told you because it's very relevant.
- Rajiv Mehta:** And can you also share the quantum of disbursement now you're doing on a monthly basis in MLAP?
- P. N. Vasudevan:** It's about INR150 crores right now.
- Rajiv Mehta:** Monthly in MLAP, right?
- P. N. Vasudevan:** That's right, monthly. And that's what, as I mentioned, that's the focus. Now the target is to try and see how that can be taken to a next level. Because the MLAP was introduced by us about 12 years back for the top end of the Microfinance borrowers. We have done a study long back. About 15% of the microfinance borrowers we determine were people who are entrepreneurs by choice, people who got into business by choice, and they were able to scale up and manage their business better and require funds to grow their business more.
- So basically, MLAP was introduced to address the top end of the MFI customers long, long time back. And -- so now what we are doing is we are getting the same MFI team to work with our current set of customer base of MFI and try and penetrate MLAP to the top end of the MFI borrowers and as the MFI loan book keeps coming down, the objective is to try and see how much of that can be filled by MLAP. So currently, the disbursement is about INR150 crores a month, and going forward, we should see how to scale that up further.

Rajiv Mehta: And sir, this net slippages being lower in the non-MFI products, so what would have driven this much higher levels of upgrades and recoveries, say, in Vehicle Finance or SBL portfolios in this quarter because the macro backdrop was not very conducive. So what do you attribute this higher recoveries and upgrades in this portfolio to?

P. N. Vasudevan: See, basically the third quarter generally is better than the second quarter normally. And -- so even our retail, our SBL businesses and all that, they really did quite well in the third quarter. Now if you see upgrades and recoveries in Q3 was about INR300 crores compared to INR216 crores in the second quarter on more or less similar level of -- no, the additional INR505 crores in the second quarter on which we were able to -- this is for Microfinance or non-Microfinance? No, we are talking of non-Microfinance.

Yes. So here you see page number -- Slide 23, we have put certain data. If you can go through Slide 23 later on, you will find out what's been the gross slippage and also the upgrades and the net slippage in the non-Microfinance portfolio. And so the non-Microfinance portfolio, the gross slippage -- the net slippage was at similar levels.

Net slippage in non-MFI was INR85 crores for the quarter. And for the previous quarter, it was INR160 crores. So there has been a significant improvement in terms of the upgrades, right? And net slippage really reduced. See, basically the third quarter is always a good quarter and fourth quarter should be generally even better normally. So we should really hope for something even better in the fourth quarter.

Rajiv Mehta: And can I just ask one last question, please.

P. N. Vasudevan: Okay, go ahead.

Rajiv Mehta: Yes. And on this credit cost, sir, so now that the SMA-2 bucket is still elevated at the bank level, SMA 0 and 1 is improving, so we will have follow-through slippages. In MFI in particular, do you plan to continue providing at 75%, 80% on the incremental slippage because your current PCL is 77%. And whether you will further utilize the remaining INR62 crores of that stressed sector provisions that you have created on the standard loans?

P. N. Vasudevan: So that usage of that balance buffer provision on standard assets in Microfinance will depend on how the bucket, that SMA buckets move in the fourth quarter. I mean, internally, we had some norms to arrive that INR100 crores in the second quarter. And basis that norm, there was a release of INR30 crores, INR30-odd crores in the third quarter.

But -- so it depends, I'm not going to be in a position to say whether we'll use it in the fourth quarter or not. It depends on how the OD bucket portfolio comes out in the fourth quarter. As far as the first question that you asked?

Rajiv Mehta: No, no, it was related to whether we'll keep continuing to provide 75%, 80% leave on the MFI business.

P. N. Vasudevan: Because what happens is our NPA norms provision, we changed it during the year for Microfinance, right? We kind of increased the provision norms, and that will continue. I mean, that's something that we are not -- actually, we are not even allowed to change it frequently. Once you change your provision loans, it will have to be on a consistent basis. So that will continue.

Sridharan N: Except the 91 to 150, rest all are 100%.

P. N. Vasudevan: Yes, 91 to 150, we are providing 50% and 150 plus, we are providing 100% and that will continue.

Moderator: The next question comes from Kamal Mulchandani from Investec Capital Services.

Kamal Mulchandani: Firstly, sir, I was seeing in the PPT that PPOP to assets is decreasing from last 5-odd quarters. So when do we see an improvement in the PPOP to average assets rate going forward?

Dheeraj Mohan: Yes. See, the factors impacting it is largely the proportion of Microfinance we have on the book. So as Microfinance is a high-yielding book and in good times, it's very, very profitable, you are seeing that impact pay-out. And directionally, we have also mentioned that we want to bring down Microfinance in the long term to some -- a single-digit number.

And to counter this movement is why we are growing Micro LAP and focusing on products which are of similar, let's say, internal ROA or internal profitability. So the whole challenge we have, and we've started this like 2 quarters back, I think is when we mentioned this, that we're growing to Micro LAP book. So the whole challenge we have is to bring back PPOP despite readjusting the bank for a lower MFI book.

So today, it's a little distorted given that Microfinance is dropping much faster and disbursement are fairly muted. So you'll have to give us some time till the storm passes, and we think that it will take another 1 or 2 quarters for us to get that clarity. So have patience till then. But these are the factors which are impacting the PPOP, it's largely that single product which is disturbing it.

Kamal Mulchandani: Got it, sir. Also, sir, if you could just help us like what would be the blended ROA for the secured book?

Dheeraj Mohan: See, this is how internal products are looked at is the transfer pricing, which happens to each of these products. So when we tell you an ROA, for example, we say that the ROA of SBL, let's say, for example, is 4% or 5%, it has a transfer pricing element of what we charge each business on their borrowings. So it's really not easy for you to understand.

All we can say is SBL is extremely profitable and there are stand-alone NBFCs, which do similar businesses and the numbers are very, very comparable. So that you should actually do a sum of parts. So what similar vehicle finance companies do or similar small LAP or NBFCs do. We are not way off any of them. We are extremely comparable. So -- and then denominator is between assets of a bank and assets of an NBFC.

So if you just adjust for that, you will actually get a better picture. But our internal ROA numbers actually will make no sense. We have given you yields of these products largely, you know the cost of funds of the bank. The cost of liability, I think we mentioned it somewhere is about 2.5% is the cost of raising deposits. So you have to adjust for all of that. So it's not a very straightforward answer, but the easiest way is to look at standalone NBFCs and do a sum of parts of Equitas.

Kamal Mulchandani:

Okay, okay. And also like what we are trying to do is that trying to understand that how the bank would again go back to 2% or more than 2% -- 2% ROA in the near future, taking into consideration that we are not increasing the share of our MFI book or even we will try to reduce our MFI share further.

So like just wanted to understand that. If we'll sacrifice on our MFI book, will it affect the ROAs of the entire bank as the secured segments are still not contributing much to the profitability?

P. N. Vasudevan:

Yes. So as I mentioned, as Dheeraj mentioned, some of our secured loan products are quite old products, and so they contribute well to the profitability of the bank.

So typically, your smallest business loan which is about 42% of the book and the used vehicles were the used commercial vehicle and the used cars, which together contribute about 17%, 18% of the book and 2%, 3% of the NBFC -- loan to NBFC. All of these are profitable at normal level because they have been around for enough time, and so they are profitable at very comparable levels.

What is still not broken even is our new products like affordable housing and the MSE that we are doing. So these two have about 12% and about 4%. So about 16% of the book is still to breakeven. And the new commercial vehicle, the new small commercial vehicle, which is about 5% or 6%, that's just at the border line.

So you are talking of really this 20%, which is either just at the border line or yet to breakeven. So these are the products which will probably start breaking even and contributing to the profitability, maybe in the subsequent years. And that is when the overall profitability of the bank can go up as these new products start contributing to the bottom line.

So Microfinance, as I said, will go down. And to that extent, its contribution to the profitability will obviously go down but some of these products like affordable housing and MSE, which have been around for the last 3, 4 years, as they breakeven and they start contributing, hopefully, some of that burden should be taken by that.

Moderator:

The next question comes from the line of Palak from ICICI Securities.

Palak:

Yes. So the question was that for the SMA-0 and SMA-1 for the MFI book are seeing some improvement in Q3 as compared Q2. So do you think that this is sustainable? Or do we think that further improvement is still expected for the coming quarters?

P. N. Vasudevan: Yes. So you're right. The SMA-0 was 2.17%. It has improved 2.03% and SMA-1 with a 1.7% has improved to 1.5%. However, if you see SMA-2, which is -- which was 2% has actually shot up to 2.73% in the third quarter, right? I think this is Slide number 25. Basically the SMA-2 has shot up because that's an effect of what happened in the second quarter, right? The X bucket flow in the second quarter will lead to an increase in NPA towards the end of third quarter, which is where we see the SMA going up.

And eventually, part of that will move into NPA in this quarter. But SMA-0 and SMA-1, the improvement that we see is because, as I mentioned, between Q2 and Q3, X bucket stabilised, even though it's not at a comfortable level, 98.2% is where it is stabilized but 98.2% is nowhere near comfortable.

At anywhere around that 98.6%, around that, we -- the MFI will actually a breakeven, meaning the credit cost that we lose and the income that it generates will kind of match each other and the product will breakeven. But if we are at any X bucket less than 98.5% or 98.6% or somewhere in the range means that the credit cost will be higher than the income generator. So net, the product will be a negative contributor.

So this first sign of improvement in SMA-0 and SMA-1 is nice, but it's really not enough. And this quarter, we have to see what is our X bucket going to be. And that will determine what will be the potential cost that we may incur over the next 2 quarters.

Palak: Okay. Understood. And if you could even touch upon what kind of X Bucket collection efficiency have we seen for the month of Jan of the MFI book?

P. N. Vasudevan: For the month of Jan, we are almost at the end of the month, of course. So we will not be able to tell you clearly because is still a few hours left for the business to wind down. But it's very similar to the last quarter, very similar and it's not shown an uptick. That's clear. It might end up very close to the last quarter.

But then there was a lot of holidays this month, hopefully, February and March with less holidays, all this have come such a big issue today that a set of holidays can tweak your performance, but that's the way it is. So January was more or less in line with Q3. And Feb and March is something that we'll have to watch out for.

Palak: So as you had mentioned in your opening commentary that maybe Q2 or Q3 of the next financial year, you would see some improvement. So 98.6% of X bucket collection efficiency is expected by Q2 or Q3 of the next financial year, right?

P. N. Vasudevan: No. Sorry, that's not what I mentioned. What I mentioned was that if the X bucket goes up in this quarter, that's the fourth quarter and if X bucket also improves in the first quarter of next financial year, then what happens is the credit cost -- see, basically, credit cost is a 6-month lag impact, okay, from X bucket efficiency to credit cost with a 6-month lag impact. So if my fourth quarter of this year, X bucket improves, then in the second quarter of the next financial year, we may see credit cost moderating, okay. That's what I mentioned.

Now what I also mentioned is that since the second and third quarter collection efficiencies have been low at 98.2%, it means that I will have an elevated credit cost in the fourth and first quarter. That's a given because X bucket was -- already has happened. So the elevated credit cost for this quarter and next quarter is a given. Now whether Q2 and Q3 of next year will be better, it's based on this quarter and next quarter's X bucket, which is where the full focus is, and that's what I had referred to.

Moderator: The next question comes from Shailesh Kanani from Centrum Broking.

Shailesh Kanani: Sir, my first question is with respect to disbursement. So in MFI segment, we have seen around 17%, 18% decline year-on-year. When do we expect this to pick up? And if you can throw some light in terms of our guidance as well because we had withdrawn the guidance of the year. Are we giving any guidance in respect to FY '26 as of now?

P. N. Vasudevan: So Microfinance disbursement will continue to be a little bit moderated only because the comfort to go all out is really not coming at. So the disbursement will continue to remain subdued. In terms of overall growth, advance growth, we have done about 14% for the 9 months period. The non-Microfinances grown by around 20%. The Microfinance was degrown by 11%. So overall, it's about 14% for 9 months. But if you ask me for the guidance, it's not going to be easy because the disbursement in Microfinance is still something that I'm not in a position to predict because if the comfort improves, obviously, the more money will go out. If the comfort remains low, then the disbursement will also remain low. So for the moment, we are really not giving the guidance on that.

Shailesh Kanani: Okay. The second question is on the used CV front, are there -- even doing affordable housing though it's a small base for us. But are there any early signs of increasing delinquencies or collection efficiency going down because that isn't getting reported in certain parts of the country.

P. N. Vasudevan: See, the collection efficiencies of commercial vehicle has actually improved in the third quarter compared to the second quarter. And typically, the fourth quarter is generally a very good quarter, both in disbursement and collections. So we expect that to continue -- that trend to continue as far as commercial vehicle is concerned. As far as affordable housing is concerned, again, our collections have been very good.

Our NPA continues to remain very much under control, and the credit cost is very at a comfortable level. And it's not small. You just mentioned it is a small part of the book. Actually, it has become 12% of the book, so it's not small, any longer. And there's no concern as credit quality is concerned in affordable housing either. Only thing as I mentioned is that it's not yet broken even. And this year, it might come very close. But next year, it should actually be positive, it should be black and that is where it should start contributing to the ROE of the bank next year.

- Shailesh Kanani:** Okay. That is useful. So just last question from my side. Is there any improvement in softer bucket resolutions? And we have kind of increased our collection team, I assume with 1,000 people coming in. So has there been any improvement? And how is the trend?
- P. N. Vasudevan:** Yes. So basically, we have increased the feet on street on Microfinance, I think nearly about 800 of the 1,000 are deployed in Microfinance. And this deployment has happened in the third quarter. And so I'm waiting to see the impact of the benefit coming in, in the fourth quarter and first quarter of next year. The soft bucket resolution, which is the SMA-0, SMA-1 and SMA-2 resolution. In the third quarter, it was not very different from second quarter, but most of the people have been joining towards the end of the third quarter. So it was too early. Even now, as we speak, people are still joining and they're getting trained, they're getting certified and then they're putting -- being put on the field. So the real benefit we should see only going forward.
- Moderator:** The next question comes from Ashlesh Sonje from Kotak Securities.
- Ashlesh Sonje:** Sir, firstly, can you just share a breakup of the net slippages in the non-Microfinance book especially across vehicle finance and SBL, both for this quarter and the previous quarter, if you can, please?
- P. N. Vasudevan:** Product-wise.
- Ashlesh Sonje:** Yes, vehicles and SBL.
- P. N. Vasudevan:** We have product-wise?
- Dheeraj Mohan:** We don't have. Ashlesh, we'll try to see how do we incorporate it in the next quarter's presentation.
- P. N. Vasudevan:** Okay. So we don't have that now. And we try and put it into our next quarter presentation.
- Ashlesh Sonje:** Sure, sir. No problem. Secondly, sir, on the MFI disbursements, they have gone up sequentially. The question on it is, at what juncture during the quarter, did you feel like ramping of disbursements? And what exactly give you that confidence?
- P. N. Vasudevan:** Actually, that was kind of outlier -- October was kind of an outlier in the disbursement in Microfinance. In the second quarter, we were disbursing approximately INR350-odd crores a month in Microfinance, it shortly was about INR950 crores. Right. So that's about INR315 crores, INR320 crores a month on an average in the second quarter. Third quarter, the October month was a sudden outlier. The disbursement was about INR500-plus crores in the month of October alone. But then November, December came back to normal level. That's why you see the blip in the third quarter. But that is not something, which is going to be repeated. And so we should see I mean as I said earlier to the previous call also, we are not in a position to predict the disbursement in Microfinance because it depends on the comfort and the performance portfolio behavior, etcetera, etcetera. But October was an aberration, and we don't expect that to happen again.

- Ashlesh Sonje:** Understood. And any specific reason for the October month being an outlier?
- P. N. Vasudevan:** Yes. I think what happened is that at the branch level, they were kind of holding back certain disbursements in the second quarter, and some of them which was being held back was actually released in the month of October. So that is why the aberration was there.
- Ashlesh Sonje:** Understood. Sir, and just lastly, out of the total Microfinance and micro loans book put together, what proportion of it would be to borrowers who are qualifying as MFI and what proportion of the MFI book is qualifying technically as Microfinance?
- P. N. Vasudevan:** Microfinance and micro loan, what proportion?
- Dheeraj Mohan:** Microloans is about 30% now. Two quarters back about 15%, now it has come to about 30% of that book. And micro loan -- 70% is Microfinance. Microfinance 70%, micro loan is 30% of the book. Both are JLG products. The products are exactly ...
- P. N. Vasudevan:** Both are JLG products. Microfinance is about 70% of the micro total book and the micro loan is about the balance 30%.
- Ashlesh Sonje:** And micro loans is essentially those borrowers where the household income could be beyond INR3 lakhs?
- P. N. Vasudevan:** That's right. Absolutely.
- Ashlesh Sonje:** Understood. Perfect. Those were all the questions I had. Sorry, if you can just repeat again, if you've shared the provision policy for the MFI book on a DPD basis?
- Sridharan N:** On DPD basis, 91% to 150% is 50%, rest all, the substandard, all the doubtful is 100%.
- Moderator:** The next question comes from CA Manik Bansal from Master Capital Services Limited.
- Manik Bansal:** So my question is on small business loans and MLAP. So what are the respective yields in every ticket size over there?
- P. N. Vasudevan:** Yes. SBL average yield is about 16%, 15.5%. Micro LAP is part of the SBL book. So micro LAP will be closer to 20%.
- Manik Bansal:** Okay. So average ticket size is?
- Dheeraj Mohan:** Yes. So INR7 lakhs below is what we classify as micro LAP. If you look at Slide 21, it will give you the SBL product mix. So today, micro LAP about 13% of SBL. So SBL is actually a collection of products.
- P. N. Vasudevan:** See, SBL average disbursement side of about INR8 lakhs. You can see that on Slide number 21. SBL is about INR7.9 lakhs is an average disbursement. And the yield on that entire book will be in the range of around 16% to 16.5%. Within that if you look at MLAP, MLAP average ticket sales should be in the range of around INR3 lakh and the yield on that would be somewhere in

the range of 22% because we have MLAP going from 20% to 24% based on different categories, different credit filters, etcetera, it ranges but the average should be around 22%.

Manik Bansal:

Okay. Okay. And another question is, like what percentage of book is linked to MCLR? Because as there is a lot of work going on the RBI cut. So what are the level the bank is going to use to keep the NIM stable or increase it?

P. N. Vasudevan:

See, we have almost 80-odd percent of the book, which is the fixed rate work, only the remaining is floating rate. Our floating rate is typically all our affordable housing is all floating rate, part of the small business loan is also floating rate. The rest is on fixed rate. And all our floating rates are linked to external benchmark, which is a repo rate. So whenever the repo rate moves, it will also move in tandem with that.

So last 2 years, we have actually seen a benefit because the repo rate had moved up, so we saw a benefit. And going forward, in case rates start coming down, then that portfolio, we should see a reduction in rate. But as far as the remaining 80-odd percent of the book is concerned, that's a fixed rate book. And so actually, on the 80% of the book, we saw a negative impact in the last 1.5 years because the cost of funds had been going up, but we are not in a position to pass it on to the old borrower.

So we were actually having a negative impact on our NIM. Going forward, just in case, the interest rate cycle reverses, then 80% of the book will continue to earn at the same level, whereas the cost of funds will start coming down over a period of time. So that will be a positive impact on NIM. So we are also eagerly waiting for when the interest rate cycle will reverse.

Manik Bansal:

Okay. Okay. And the last question is, like which segments according to you are the highest growth contributors for the bank?

P. N. Vasudevan:

See, for us, the flagship product is a small business loan because it is sitting on a very high level of unmet credit demand from the market, and it can sustainably grow around the 25% to 30% level. We have been doing it for a long time, so we do know how to handle that product. The competition from the mainstream banks is not high because the product is inherently difficult to handle, and we have a lot of competitive strength built up over the year. And that product has seen all kind of headwinds starting from GDP growth. GDP cycle is going up and down, Demonetization happening, corona happening. It's been all kind of headwinds, but the credit cost and that has never gone out of hand, never ever gone on our hand. So that remains on the flagship and we'll continue to be high-growth products for the bank. The next one will be our used commercial and the used cars, which is also -- used commercial of course, is a 12, 13-year old product in the bank. Used car is about 4 years or maybe 4, 4.5 years old. And both of them also will remain a flagship growth product for the banks because they tick all the parameters.

Affordable housing will be a third focus product for the bank. Because it performs very well from a credit quality perspective. The only thing is that it is still not contributing to the bottom line. And hopefully, next year, it should start contributing, but it ticks very strongly on the credit quality. So that will be a third focus product for the bank.

- Moderator:** The next question comes from Amit Mantri from 2Point2 Capital.
- Amit Mantri:** Yes. Can you -- if there is any change in the yield that is being charge on Microfinance loans?
- P. N. Vasudevan:** See, earlier, we used to have a flat rate. Now towards the end of last quarter and this quarter, we have introduced our slab-based rate. So the rate stats from 20% and goes all the way to 25%. So it depends on the profile of the borrower. So people who have been with us for 2 cycles, 3 cycle, 4 cycle, etcetera, they get a lower rate. People whose past track record has been very good with us, they get a lower rate.
- People whose attendance at centre meetings have been beyond certain minimum level, they also get a lower rate and so on. So we have defined a few set of credit parameters. Those who tick all the boxes can get the rate as low as around 20%. And those who don't tick any of the boxes will go at the highest slab, which is around 25%.
- Amit Mantri:** So what would be the impact of this introduction of slab-wise system of rates going forward? Will the average interest rate on Microfinance loans decrease because of this change?
- P. N. Vasudevan:** Yes, it should. So we did try to do some simulation on that. And I think it might reduce the yield on Microfinance by anywhere around 1.5%.
- Amit Mantri:** 100 basis points to 150 basis points basically.
- P. N. Vasudevan:** That's right.
- Moderator:** The next question comes from Rajiv Mehta from Yes Securities.
- Rajiv Mehta:** Yes, just a couple of follow-ups. Sir, even affordable housing disbursements the traction you see lower in terms of run rate versus last year. So there was supposed to be a pick up, but we haven't seen that pickup in Q3. So Q3 number of -- Q3 figure for disbursement is also lower on Q-on-Q basis. So what is happening here? And when do we see going back to the levels of disbursements which we were doing last year and then even higher subsequently?
- P. N. Vasudevan:** Yes. So the disbursement in Q3 is lower than every other quarter. It's lower than Q2. It's lower than Q3 of last year also correct. Lower than Q3 of last year, it's lower than Q2 of this year also. It's only better than Q1. Q1 was the very bad quarter, it's only better than Q1. Basically, in affordable housing finance, our disbursement yield, there is a conscious effort by the team to improve the disbursement yield in the affordable housing space.
- And we had initially, our whole affordable housing started from Gujarat and then Maharashtra. And subsequently, we came down to South and we put up operations in Tamil Nadu, Karnataka and APT. And so the team's effort -- in their effort to try and improve the yield of the disbursement in affordable. They actually took a call to slow down part of the disbursement from West and trying to improve the disbursement from South, and that's why you see the disbursement coming down. But in return, the yield actually has started going up even in the

third quarter. And going forward, the focus will continue to be try and have a blended yield between South and West, between self-construction to flat purchase to builder purchase.

So there has to be a proper mix amongst customer profile as well as property profile to ensure that our yield is maintained while growth is also taken care of. So that's a kind of fine balancing that the team is trying to do, and that resulted in this dip in the third quarter. But hopefully, they will be able to come out of it, maybe even this quarter.

Rajiv Mehta: And just on Slide number 26, you mentioned about additional provision. And I think you've also made the -- I mean it's mentioned in there that there is a INR16-odd-crores of additional provision done in Q3. Now what -- so where is that INR16-odd crores of provision? I mean is it in the PCR of MFI or -- because you actually utilized the standard funding provision that you created last year. So what do you mean by the recent provision of INR16 crore done in Q3?

Sridharan N: The additional provision is in respect of the bucket -- the provisional changes in the bucket of MFI from 151 to 180 earlier, we are providing 75%, we started providing 100% now in Q3. That's the incremental provision in Q3 -- in Q3 FY '24.

Rajiv Mehta: Okay. Okay. And that's a change in policy itself now. So even on a continual basis, 150-plus crores will be 100% provided?

Sridharan N: See, this is a change in -- change from the bank policy of earlier follow. So it will be consistently followed in the future.

Moderator: Ladies and gentlemen, we would take that as a last question for today. I would now like to hand the conference over to Mr. P. N. Vasudevan for his closing comments.

P. N. Vasudevan: Yes. So thank you. Thank you all for dialling in, listening to us, asking us questions, and helping us to understand our business better. And we look forward to meeting all of you guys again next quarter. And hopefully, the performance also should be much better than what's happening now. Let's hope that the market stabilizes, market settles down, customers come back to more normal levels of behavior and things do get back to some level of normalcy. Thank you, and we wish you all the best. Bye.

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