2nd February 2023

BSE Limited
25th floor, Phiroze Towers,
Dalal Street,
Fort, Mumbai- 400001

National Stock Exchange of India Limited
Exchange Plaza, 5th Floor, Plot No. C/1,
G Block, Bandra - Kurla Complex,
Bandra (E), Mumbai - 400 051

Scrip code: 511742

NSE Symbol: UGROCAP

Subject: Transcript of the Earnings Call with Analysts/Investors held on 27th January 2023

Dear Sir/ Madam,

Pursuant to Regulation 30 of the SEBI (Listing Obligations & Disclosure Requirements) Regulations, 2015, please find enclosed the transcript of the earnings call held on 27th January 2023 to discuss the unaudited financial results for the quarter and nine months ended 31st December, 2022.

The said transcript is also being uploaded on the website of the Company.

This is for your information and records.

Thanking You,

Yours faithfully,
For UGRO Capital Limited

NAMRATA SAJNANI
Digitally signed by NAMRATA SAJNANI
Date: 2023.02.02 14:45:43 +05'30'

Namrata Sajnani
Company Secretary and Compliance Officer

Encl:a/a

"U GRO Capital Limited
Q3'FY23 Earnings Conference Call"
January 27, 2023

MANAGEMENT: **MR. SHACHINDRA NATH – VICE CHAIRMAN AND MANAGING DIRECTOR**
MR. AMIT MANDE – CHIEF REVENUE OFFICER
MR. ANUJ PANDEY – CHIEF RISK OFFICER
MR. KISHORE LODHA – CHIEF FINANCIAL OFFICER
MR. NIRAV SHAH – CHIEF STRATEGY OFFICER AND HEAD OF INVESTOR RELATIONS

Moderator: Ladies and gentlemen, good day, and welcome to UGRO Capital Limited Q3 FY '23 Earnings Conference Call. 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, please signal an operator by pressing star and then zero on your touchtone telephone. Please note that this conference is being recorded.

From the management team, we have today, Mr. Shachindra Nath, Vice Chairman and Managing Director, Mr. Anuj Pandey, Chief Risk Officer, Mr. Amit Mande, Chief Revenue Officer, Mr. Kishore Lodha, Chief Financial Officer, and Mr. Nirav Shah, Chief Strategy Officer and Head of Investor Relations.

With that, I now hand the conference over to Mr. Shachindra Nath. Thank you, and over to you, sir.

Shachindra Nath: Good evening to all participants. Thanks for spending time to listen to our results for this quarter. We have delivered as per our plans, which has been made public. But before that, for those who might be joining new, I would like to take you through the journey of U GRO in few words. U GRO was set up as India's first listed vehicle, which is started fresh.

We acquired a small listed NBFC in 2018, and raised approximately INR 950-plus crores of equity capital from globally-acclaimed private equity investors. We started our lending journey in Jan 2019, which was just post IL&FS crisis. In three years of our inception, we have seen through many other crises, like DHFL, Yes Bank, COVID and all other kind of other challenges for FinTechs and NBFC.

For all of us here and for our customers, this has been one of the most difficult time. Still, we have persevered and crossed the milestone of INR 5,000 crores of assets under management and 38,000 customers, maintaining the credit cost under control. This, among our peer set, is the most accelerated build-up of a lending business, in this segment. This is the result of overinvesting in our operating infrastructure, data analytical infrastructure and distribution architecture, and we are seeing the results on asset growth and bottom line performance.

Since our inception, we were and continue to be, of the opinion that India's small business lending is at inflection point of explosion. We have seen a 1.5 decade of consumer financing growth. And now you would see a similar growth for small business financing.

This is happening on the back of being able to underwrite an SME customer, through the lens of fast emerging data stack underpinned by GST, digital banking, maturity of bureau, coupled with deep data analytical progress, which can underwrite the cash flow and not just the collateral.

In addition to this, we believe that every small customer is different, and they are not homogenous. Therefore, you have to evaluate them with sectors and sub-sectors. We therefore built our credit scoring model, GRO Score, which uses the data of GST, banking and bureau and our underwriters use our sector and subsector-based templated underwriting scorecard.

We have one of the largest data analytics and technology teams, for a company of our size and vintage. We always believed that data and technology will drive the MSME lending in India and true to our belief, the entire ecosystem is now transitioning to an on-tap financing similar to what we have seen in consumer lending many years back. Our credit scoring model, which provides a decision within 60 minutes is now well accepted across lenders and our co-lending partners.

In last few calls, I did mention that India's NBFC lending model is transitioning from an on-balance sheet to an off-balance sheet lending. And U GRO is leading this transition as a leader. So on one side, we have the strength of serving the MSME through multiple product, and on the other side, we have our co-lending and liability partners. We have been investing heavily in teams and distribution network and taking all the costs upfront by creating a franchise which has a strength to now originate loan in excess of INR 600 crores per month.

Banks lending to NBFC like us will take another shape in the form of co-lending and here again, we have seen the changes over the last many months. We continue to maintain a healthy mix of on-balance sheet and off-balance sheet risk by sharing our co-lending and co-origination partnership with more than 10 of the large banks and multiple large NBFCs.

As we speak, our off-book AUM ratio has reached 35%, which we had targeted to achieve by March '23. With respect to the on-balance sheet liability, U GRO is one of the few companies, who have been backed by 65-plus lenders, in a short span of time. Our total off-book volume was INR 724 crores compared to INR 590 crores in Q2.

The breakup of INR 720 crores was co-lending of INR 273 crores, direct assignment of INR 108 crores, and this was supported by co-origination of INR 343 crores. Income of co-lending and direct assignment is recognized upfront, on the basis of discount rate. However, for the co-origination incomes, it accrues to us over life of loan as if the loans were on our balance sheet.

Over our four-year journey of precise execution and a process-driven approach, U GRO, today, has become a large-scale MSME lending platform, comprising INR 5,000 crores of asset under management, INR 1,800 crores of quarterly disbursements, 100 branches, 38,000 customers and more than 1,500 employees. While our numbers have been made available to you, I would share few highlights.

Momentum in growth of AUM and disbursement, our total AUM increased to INR 5,095 crores from INR 4,370 crores in last quarter, up by 16% quarter-on-quarter. We have recorded the highest ever disbursement in Q3, which is stood at INR 1,874 crores for the quarter, which is 13% higher than the last quarter.

Growth in terms of the total net income, our net total income has increased to INR 108 crores for Q3 versus vis-a-vis 24% in Q2 '23. As a percentage of on-book AUM, the net total income increased to 12.9% from 11.3%, in last quarter. Our opex and cost-to-income ratio stood at 63.9% in Q3 '23 as compared to 62.7% in Q2 '23, primarily on account of certain one-off expenses being recognized in the quarter.

Adjusted for this one-off expenses, our cost-to-income ratio would have been around 60%. The employee cost month-on-month basis have been stable. \

Our path to the higher RoA and RoE and profitability, the trend is very clear. Our PBT has increased to INR 22.2 crores in Q3 '23, registering a 27% quarter-on-quarter growth. And our PAT for Q3 '23 stood at INR 13.1 crores, registering a 149% quarter-on-quarter increase. Our cost of borrowing has seen no significant increase. We have a very well-diversified base of 65-plus lenders, including some of the largest banks in NBFC.

While the cost of borrowing has remained at 10.5%, for most of the other players, it has increased by 100 basis point or more, while our cost has increased only by 20 basis point in last two quarters. And the last but not least, the disbursement in the Lending-as-a-Service or what we call the co-lending model, we have seen our total off-book portfolio increase to INR 1,775 crores, which is about 35% of our total AUM.

We have started to see the result of the scale and liability franchise that we have created. Efficiency has started building out in our network and same has started to reflect in our profitability on quarter-on-quarter basis. Despite demonstrating higher growth and improving profitability, the capital market seems to have not looked at the potential of our platform over the next two to five years. This might be because of our lower market cap, coupled with capital markets have been muted for lending businesses and our differentiated lending model not fully propagated among institutional investors.

We have proven our asset engine, its growth potential, our credit engine, and its ability to control credit costs and now our focus for next year will be delivering profitability, which is comparable to any traditional or vintage lender. This, we believe, would put us in the bracket which is superior to banks and traditional NBFC.

We have demonstrated that from the last year PBT of INR 20 crores, this year at nine months itself, we have reached INR 50 crores. But now we will focus on doubling the bottom line over next financial year, while asset engine would continue to grow. It takes a lifetime to build financial institutions.

We are toddlers vis-a-vis some of the other institutions in our industry. But with a deep sense of responsibility, we say that we are committed to build India's largest small business financing platform, serving the need of the customer, who otherwise do not get access to credit. And in that journey, we would build a financial profile with consistency, which only few have ever achieved.

Thank you for listening to us. We are here to answer any question which you may have. Thank you.

Moderator: Our first question is from the line of Satish Kumar from Choice Equity Broking.

Satish Kumar: So my question is about incremental disbursement. So over the last few quarters, we have seen incremental disbursement to the supply chain financing has been increased compared to other prime unsecured and secured segments. So can you throw some light on this, sir?

Shachindra Nath: Your question is that you are seeing the growth in our disbursement? Or is anything specific.

Satish Kumar: Incremental disbursement for supply chain financing segments has been increased over the last few quarters compared to other segments like prime secured and prime unsecured segments?

Shachindra Nath: Yes. I'll give you headlines thinking about why it is happening and Amit can take you through further. Look, as you would see our last three-year journey, and you look at our distribution model and our risk profiling of our portfolio, we started with prime segment to begin with. We started with eight location prime businesses supported by 500-plus intermediaries and then over a period of time, we implemented multiple other channels.

So then within our branch infrastructure, we opened roughly around 75-plus micro enterprises branches. Each of these branch take roughly around 18 months to get to a level of breakeven and then they start throwing assets from that point onwards. We then establish our ecosystem channel, which is the machinery financing and supply financing, our partnership analysis channel and digital, which will go live soon.

So it is the evolution and very heavily investing into multiple distribution channels, and they are now matured and - that's why the benefit is coming now. As time passes, each of our channel would grow. And also, you would see the yield profile of the company improving because most of our channels are secured and higher-yielding segment.

And also now, we have established our data analytics and GRO Score far more because we have a track record of almost now three years to 3.5 years. So that is also helping us to grow all of our channels. Amit, if you want to add something?

Amit Mande: So, Mr. Satish, thank you for the question and thank you, Shachin. While you've covered that all our channels are now really coming up the curve and really being able to service all kinds of needs, supply chain is a very peculiar channel that we want to focus on because that really services the short-term need and typically in these seasons, which are festive seasons, one would see that the supply chain demand is extremely high.

We've been servicing this demand over last quarter and this quarter again. And so the disbursement in this channel has seen significant growth. However, this will also remain our key channel to service multiple focus sectors, like green energy, like wash, like healthcare, and we will continue to focus on this channel and in future as well, this will remain a significant contribution of our disbursements.

Satish Kumar: And, sir, my next question is about the operating expenses. So the cost-to-income ratio is around over 60%. and it's a meagre share of our income. So when should we expect this to normalize going forward, sir?

Shachindra Nath: So, sir, the way I think so, we have expected capital market to be cognizance of the fact that you are seeing a company with a three year vintage, started at ground zero. When we raised our capital, we had not a single person in the company, nor a single loan. Most of the time, what you are seeing in listed world is companies which operate as unlisted for at least five years, seven years, 10 years and get to a level of maturity and then come to the market.

And that's why you pay them an X amount of premium. So we have established our business right from day one in the opening glare of a listed market and invested very heavily in the opex. So these our numbers are not comparable to most of the our peer set, but obviously, you don't have to worry too much about it because you have choices to make, as when you board an aircraft, the pilot says that you have many airlines to go on. So you'll choose what provides you the best.

But you also think in terms of what would take you to your destination with safety, vis-a-vis many of our peers, which actually, in the initial first five years, bleed on the bottom line. So they burn capital and then come to a breakeven point and operating profit.

We have been profitable from day one. And also, we are competing head on to come to a cost-to-income ratio, a return on asset and return on equity, which is equal to or better than most of our peer market. Our year beginning cost-to-income ratio was 72%. It is now at 60%. So all of our opex is now more or less complete. And what you are seeing is only the growth on the asset side.

So with every passing quarter, this would continue to improve. I have said in my opening remarks that from a INR 20 crores of bottom line, we have now delivered INR 50 crores of PBT in the first nine months and our endeavour would be to double it for the next year. I did say, if you look at our quarterly presentation, we have said that, in 2025, we'll be at cost-to-income ratio of roughly around 45%, which is the best in the market.

Moderator: We'll take the next question from the line of Sheetal Gawde from ULJK Financial Services.

Sheetal Gawde: So congratulations, sir, for great sets of number, finally you achieved INR 5,000 crores of AUM milestone and we are sure that by '25, you can easily achieve INR 20,000 crores in your milestone. So I have some couple of questions on the yield side. As you are focusing on the off-balance sheet portfolio, around 50% by FY '24. So currently, the yield on portfolio, which is a total of on-book and off-book is around 17.4 percentage.

So I just wanted to know because the liability side is diversified, so that is the reason you can sustain your cost of borrowing. But I just wanted to know on the yield side, how is your view on a future that if you're focusing on the off-book, which is obviously it's a high-yield business, so going forward, how you're looking on the yield side on portfolio side?

Shachindra Nath: Sir, sorry, off-book to on-book, yield on portfolio has no difference, right? So when your yield of portfolio is at what rate we lend to the customer, right? That is independent of when we are lending to the customer. Whether the asset is going in my balance sheet or is it going to a co-originating partner or it is going to a co-lending partner, yield on the portfolio is yield on the portfolio, right.

Sheetal Gawde: So just wanted to know that what is your expectation like going ahead by '24?

Shachindra Nath: So as I was answering the question from Choice Broking, that our prime business which is technically a lower-yielding business is now, in terms of the percentage terms, it is roughly around 50% of our monthly volumes. But our higher-yielding business, micro enterprises, the machinery business and few others, are now gradually growing.

So we expect and we are not making a prediction, I said that we will endeavour to double our profitability, and that's a combination of opex remaining flat, credit cost remaining same, stable and flat and our portfolio yield gradually going up and AUM growing up to double the profitability. So I think so it's very difficult sitting here to predict in percentage term what would be the yield increase on the portfolio. But definitely, there'll be an inching up which will happen now.

Sheetal Gawde: Great. And the second question is on NPA side. So now obviously it's a only two, three years of operations of U GRO. So currently, it's like very nominal GNPA and NNPA. So now the company is focusing on the AUM growth part. Because the narrative of AUM is the secure, right? So how going forward you are expecting that the NNPA will be by '25?

Shachindra Nath: Anuj, do you want to take this?

Anuj Pandey: So the overall portfolio quality is a function of the overall portfolio mix as well as in individual business lines, what is the expected GNPA. So with our statistical scoring models now quite stable, we are in a position to somewhat predict of how the portfolio will behave.

As you would and we have been reiterating this in previous calls as well, the endeavour is to have a healthy balance in the portfolio with secured book overall to be around 70% and unsecured book to be around 30%. And the projected, if you see our five-year plan, the projected gross NPAs are not likely to be over 2%. And the way things are, and we have seen the early warning signals and early indicators of the portfolio, we think we would remain within that.

Sheetal Gawde: And last one is on the capital raise. Like in the last three years, you raised around 30 billion through equities and debt. So going forward, because now that U GRO is focusing on off-book AUM, so now is there any plan in one year down the line for any capital raise?

Shachindra Nath: So we have already disclosed at the beginning of the year itself that by end of the quarter, which is the fourth quarter of this year or the first quarter of next financial year, we would be doing the capital raise. Its form, shape and size is not yet defined. But at the speed, at the growth rate which we are, we would definitely be raising capital.

Moderator: We'll take our next question from the line of Ankur Kumar from Alpha Capital.

Ankur Kumar: Congrats for a good set of numbers. Sir, you talked about safety and in the line of that aeroplane. So I just wanted to ask because we have grown to INR 5,000 crores in about 3.5 to four years, and we have good targets for coming two years also. So, but this fast-growing is generally considered not so safe in the financial institutions as in from the capital markets' perspective. So how do you think we are going to manage in terms of both growth as well as managing the NPAs?

Shachindra Nath: So the answer to this is that, sir, if you look at -- if you compare us with 10 other NBFCs, which are in micro enterprises segment, there is not a single one which started with a total capital at the day one of INR 950-odd crores. So we have recently seen Five Star going IPO. Five Star to reach at the scale where they are, have taken 15 years, but it is not because the wider the capacity was a problem or the market opportunity was a problem or speed was a problem.

It is because they started with only INR 25 crores of capital. And to get to the base of capital where we are, it takes roughly around ten years. So the fast growth is not a function because we are disbursing money recklessly. So right from our day one, the log-in to disbursement rate for U GRO has been stable at 30%. For a INR 400 crores worths of loan, we originate INR 1,600 crores every month. It is a function of the capacity which we built first three years, and that is what is affecting the volume, and that's what's maintaining the credit quality.

So this business in at the end of 2020 had only 150 people, eight locations. At the end of 2022, it had roughly around 1,500 people, 100 locations, 150 people in technology, 40-plus people in data analytics. So our growth and we are not chasing growth, actually, our installed capacity versus what we are delivering, we already have a gap of 30%, 40%.

So we are not chasing growth, growth is coming because all our verticals have been deeply established with both people, technology and credit processes. There'll be definitely a point of inflection after which the company would grow at 15%, 20% per annum basis. But till that time, the base effect of our infrastructure will deliver the growth.

Ankur Kumar: Sure, that's great to know, sir. And sir, in terms of tax rate, this quarter we had high tax rate. So can you explain why and what is our expectation for the tax rate in the coming years?

Shachindra Nath: Kishore, you want to take that?

Kishore Lodha: So it is largely because of two factors. One is that since we are into MAT, we are still into the old regime, so which is higher compared to the normal tax rate. And also during the merger of Asia Pragati, we have inherited some carry forward losses, where we have created deferred tax assets, some of which has got lapsed during the period, and hence, we had to reverse those losses. So in H1FY23, we have taken a hit of around INR 7.2 crores.

And we have incrementally made provision of around INR 4 crores during this quarter. So cumulatively, in YTD December, we have made additional provision of around INR 11.3 crores on deferred tax asset which was created earlier and now require reversal. Otherwise, we would have been in normal stable regime of 30%, which is in line with the old regime of taxation. We are into MAT, hence, we have not migrated into the new tax regime.

Ankur Kumar: So how much of this deferred tax asset is still pending, sir?

Kishore Lodha: So deferred tax asset is pending in the books is roughly around INR 17 crores which is available for over next two to three years and one would be available till next 7th years. Part of it, we should be able to utilize. But a part may again, we may have to take a reversal in coming quarters.

Ankur Kumar: And sir, one question. In terms of coming 12 months, what are the risk that we see in terms of achieving our guidance in terms of doubling of the profit before tax and growing AUM that far. So what are the risks that we see in the business?

Shachindra Nath: So we operate in the customer segment in the loan ranges of INR 10 lakh to maximum INR 3 crores, unsecured loan only maximum of INR 25 lakh segment. Generally, all of this noise of about inflation, economic slowdown, Ukraine War and all of that, we believe that, to a very large extent, the micro enterprises segment is [technical glitch] and micro-economies.

And also, we are not seeing a major economic slowdown to happen in India which can cast it to the bottom of the pyramid. So generally, from the customer segment in which we operate, we are seeing very healthy growth for all our segments of the market.

Having said that, as in financial institution and as a lending institution, this increased rate scenario is obviously of a concern because if our borrowing rate consistently keep increasing, then obviously, that's a problem because our customer finally cannot afford a very high cost because they have a very limited margin. But good thing or good story about it is that we are now seeing the rate hike to taper down, and we are only hoping that only one or two hikes to happen more.

Second, I think so that generally, the liquidity in the banking system has reduced because the credit demand has been extremely high. And obviously, as you know, we are largely dependent upon banks and also the capital market, public market, DFIs. But we are not growing by INR 25,000 crores a year. Our growth rate and number of satisfied lender, we think that is also not a big challenge, but that's also continuing to be a risk for the broader market.

Ankur Kumar: And sir, in terms of secured book, you're saying 70% book is secured, what is our LTV on that book?

Shachindra Nath: Anuj, you want to take that?

Anuj Pandey: So it is divided between secured-by-property and secured-by-machinery, primarily. So in secured-by-property, our average LTVs are around 55%. And on secured-by-machinery, our average LTV would be around 65% to 70%.

Ankur Kumar: And sir, last question would be, as in you talked about capital markets not appreciating our journey so far. But we have lot of PEs on the Board. So what is exactly that they seem to be thinking that we are missing because of which capital market is not appreciating us?

Shachindra Nath: So as I said, that there are multiple reasons and very difficult to specify. But first and foremost reason that we emerged just prior to ILFS crisis and capital market has seen multiple financial institutions to be under trouble, DHFL, Yes Bank, so on so forth. Then capital markets saw a massive wave of COVID, which affected the lenders generally.

So I think so those elements itself, while there was a broader rally in all other sectors, banking and NBFCs had not seen a rally. Now we are seeing little bit of a rally happening only for top-Tier private sector banks, but there are also many number of banks and NBFCs, which are what we call the traditional and legacy, which are also available to public market at a very reasonable price.

I think so, look at it this way, if we would have done an IPO now or two years down the line, you guys would have paid a value which would be 4, 5x higher than what we are today. But we are okay with that. But eventually, our moderning superiority on a lower capital base, being an entity, which is being able to generate much higher ROE would get appreciated.

So no businesses, which are superior to their peer set can remain out of mainline radar for a very long period of time. And we are making a conscious effort for broader market to understand us better.

Ankur Kumar: And in terms of closest listed competitor, would we call Five Star as our closest competitor or...?

Shachindra Nath: No, sir. I think so that -- I think we are in the domain of FinTech and FinTech credit platform are yet to be listed. Paytm was the last and BankBazaar was the last FinTech which got listed, but both of them were non-credit businesses. And both of them went to the market on metrics of listing which are at least I don't understand.

So if you look at our asset profile and our business profile, we don't have a direct peer set. So our prime business compete with the bank, our microenterprise business compete with Five Star, Vistaar, Veritas, our supply chain finance business see a compete with global FinTechs, which are in supply chain, our machinery business compete with Electronica and others, our P&A business is similar to that would be a Max Financial, which is a listed.

And when we launch our digital channels, that's will be a completely FinTech platform. So I think so, we are creating a category of India's largest small business financing platform driven by data and tech. So we hope that others would also follow. It is very difficult to say this is our listed nearest peer. But only from a valuation perspective, while we are big, broad, diversified, so it's monoline business or where they are, so obviously investors have to make their choice.

Moderator: Our next question is from the line of Akash Jain from Ajcon Global Services Limited.

Akash Jain: Congratulations, sir, on a very good set of numbers. My question pertains to the growth for FY '24, like, AUM target, we have around INR 7,000 crores. So predominantly, we have shortlisted around 8 to 9 sectors and exposed to those accounts which have a credit history. So are we looking to broaden our sectoral outlook beyond those 9 sectors?

Shachindra Nath: Anuj?

Anuj Pandey: So when we had selected these 8 sectors and then we added a 9th sector called Micro when we started the business, they were actually pretty large sectors in themselves and contributed about 45% to 50% of total SME GDP. And now we are seeing traction overall and the buoyancy. If you recall, our 8 sectors, 3 are quite service-oriented and 5 are mixed, all towards consumption.

We are seeing very good growth in these sectors. And at this point in time, we don't see any reason why we should add. But in case there is some opportunity which comes in where we see a lot of potential, theoretically, we are open, but at this point in time, we would like to focus on these 8 sectors and keep building our expertise.

Akash Jain: And secondly, on the commitment of the private equity players. So is there any like outlook of the private equity players to stay with the company?

Shachindra Nath: So, sir, any investor, whether it is a private equity player or a public market investor, have the flexibility and freedom to come and go, right? And that is the way we would like it to be. Like in an HDFC or ICICI or large platform, investors come and go, the platform or the institution should stand on its own. Having said that, we started with four private equity investors, of which three of them continue to sit on our Board.

And we are still within their investment cycles, and there is a long residual fund life. So we think to that, when they'll be near to their fund life cycle, they'll gradually divest, but that is not happening today. So let me add this. As you know sometimes, I've seen sell-side analysts asking this question that what would happen when these large investors would sell.

See I've taken the case, example of, say, AU or few other large NBFCs, institutional ownership through private equity is very common now. But normally, these ownership don't come into the public market. So there are larger financial institutions, which would like to come and take over some of these shareholdings. So today we have four Asia private equity funds in our business, but there are then large funds, Sovereign and others, both active and passive. As we continue to grow in size, they like to start or they would like to participate in platform like ours.

Akash Jain: My other question is on the GNPA and NNPA ratio. If not for this fast AUM growth, what could have been our GNPA ratio and NNPA ratio?

Shachindra Nath: Anuj?

Anuj Pandey: So basically, you are referring to our static pool delinquencies by vintage. And we keep monitoring that, they wouldn't have been too different. So the post-pandemic sourcing, post-July 2021 when we implemented our new GRO Score 2.0, which took into account both the banking behaviour and repayment behaviour by sector, we are seeing that even after 12 months, 18 months, the book quality remains consistent. So it wouldn't have been too different.

Moderator: Our next question is from the line of Nirvana Laha an Individual Investor.

Nirvana Laha: So the first is a bookkeeping question. So for the nine months of FY '23, I can see that the total comprehensive income is about INR 25.4 crores. But the equity from March '22 on the books to now has only increased by INR 2 crores. So how are we accounting for this?

Kishore Lodha: I'll take this. Your question is right that while our profit has increased, it is not reflecting into our total equity. Because if you remember, last quarter, we have done a setup in ESOP trust where we have purchased share of worth INR 25 crores, which was adjusted with the capital. Hence, with this adjustment, it is what it is.

Nirvana Laha: And is this trend likely to continue? So when will we see the book value increasing through profits flowing through to it?

Shachindra Nath: In our public disclosure, the ESOP trust approval is for roughly around INR 28-odd crores, of this, INR 25 crores has been exhausted, so rest of it will get exhausted as and when the trust decides, that's an independent offer. But we should see now, with every passing quarter, we should see accretion on the net worth of the company.

Nirvana Laha: So the next question is regarding the deferred tax assets. So Mr. Kishore, you said that INR 17 crores were still left from that demerger. Can you tell us what percentage of the INR 17 crores is likely to lapse again and hit the PBT? Because this number is affecting our ROEs clearly, so a clear guidance on that would help us module things?

Kishore Lodha: So as we move forward, depending upon the profitability, whether we will be able to absorb it or not will depend upon the what kind of profitability we will have in future. But clearly, we can foresee that, next year, our deferred tax liability, which is about to lapse is close to INR 7 crores.

In our belief, with the profitability target, which we have in mind, we should be able to absorb that. So there should not be any impact on PAT next year on this line. And then there is another line, another deferred tax asset, which is there, which is roughly around INR 2.3 crores, which will be lapsing some around 2029, '30 so that much will be unlikely to impact because by that time, our profit will be very high and probably we will be able to absorb it next year or the year after.

There is one portion left which is available, which will be lapsing this year itself. A part of the provision we have done in this quarter and the balance portion, if the profitability, we are not able to absorb in next quarter, then this one that part we will be taking in the next quarter.

Nirvana Laha: How much is that, may I know?

Kishore Lodha: I will have to check and get back on the same.

Nirvana Laha: I'll connect offline on that. Secondly, on your projections for FY '25, you have given two ratios this time, which is PBT by average total assets and PAT by average total assets. So if I look at the PAT to PBT ratio there, it's coming to around 18%; 4.5% divided by 5.5%, that's around 82%. So does that mean the normalized tax rate for U GRO going forward is going to be in that

18%, 20% range? Or are you factoring in some deferred tax assets reducing the effective tax rate?

Kishore Lodha: So it will depend upon two factors. One that as I explained earlier that we are into MAT as of now. So whatever provisioning we are doing, it is on account of deferred tax. So going forward, if the profits are there and we are able to absorb the MAT bracket which is available, depending upon this factor, the final tax rate would arrive at that point of time.

Nirvana Laha: So as an outside investor, I should go ahead with 25% as the effective tax rate?

Kishore Lodha: Not exactly, because again, MAT credit is easily available, so it will be available for utilization in '24-'25.

Nirvana Laha: I'll connect with you offline on this, Mr. Kishore. I have a few questions on collection efficiency. So the same-month collection efficiency this time is around 94%, and it's consistently at that level. So I was just comparing the collection efficiency with banks. I know Mr. Nath has earlier said that that may not be the right way to look at MSME collection efficiency, but still wanted to just get a confirmation that the 6% that is flowing into buckets, how will this resolve into NPAs?

I know that this was explained in the last call, but 6% optically, when I benchmark with banks, which may not be the right benchmark and so I'm asking for this guidance, it looks like it could translate into higher than 1%, 2% NPAs. But if that is not the case for our kind of lending, I would just like you to explain that, please.

Shachindra Nath: Sure, so I was answering this question that our 94% collection efficiency, what you're comparing with the bank is - ours is 98%, right? So total collection, which is including overdue versus current month demand is the way most of the NBFCs and banks report, that is at 98%. Now Anuj, can you take this 94% and what happens to the 6%? And how but, is that the right way to think that the 6% is all flowing into NPA?

Anuj Pandey: Yes, I'll take that. Thanks, Shachin. So typically, collection efficiency numbers should be seen in conjunction with the subsequent bucket resolution numbers. So when an account bounces the check for the first time, it moves to what in industry is called Bucket X and the Bucket X resolution rate is the primary driver, along with collection efficiency on what would flow further.

Typically, in our case, because it's a small business lending, the Bucket X solution rates are closer to 98%, 99%. And hence, whatever is flowing forward is close to 1% and 1.5% only, which will eventually can become NPA. So a collection efficiency number, along with the Bucket X resolution number, will normally give the full picture.

Nirvana Laha: On the co-origination book, so what is the percentage of FLDG that we usually have to provide?

Shachindra Nath: So it varies, right from 3% to 7.5% is the first loss cover on co-origination with other large NBFC we have provided for. But the losses would be similar to what is on our balance sheet. So

I think so, whatever you are seeing in our credit cost is the total credit cost which is right now its current flow were presuming 2.5%.

Nirvana Laha: I see. And this is only applicable for when there's an NBFC on the other side of the transaction, not when a bank with them?

Shachindra Nath: Banks are not allowed to take FLDG as per RBI circular.

Nirvana Laha: And could you tell me, out of the INR 74 crores total provision, how much of it would be towards covering the FLDG guarantees?

Shachindra Nath: Very, very small. Anuj, you have that number?

Anuj Pandey: So the provision is the way if the co-origination business would also have been booked on our own book. So there is no difference. It is just that we cover it adequately by the way we do it in Stage 1, Stage 2, Stage 3. So at this point of time, the coverage would be in line with that product. Typically, our Stage 1 provision for unsecured loan is close to 1.5%. For a secured loan, it would be around 1%.

Nirvana Laha: So the reason I was asking was, today, the provision is 1.5% of on-book AUM. So after removing that number, I just wanted to check what the provision to AUM ratio would come at. But I can write to you offline and get that number. So last question from my side...

Shachindra Nath: So I give a bit, our provision includes the book which is co-originated book. So if I have a INR 100 of book of on-balance sheet and INR 100 book on co-originated, we presume as if we have INR 200 of total book. And when we provision, we provision as Stage 1, Stage 2, Stage 3 on the total of INR 200.

Moderator: Our next question is from the line Joel Elias, an Individual Investor.

Joel Elias: Congratulations on the numbers again. I just had a couple of questions regarding the customer journey. So do we have any KPIs for evaluating customer stickiness, customer satisfaction and customer retention? I wanted to know if we are aggressive with trying to get customers to borrow repeatedly as in, what is our approach towards customers? And how do we evaluate that?

Shachindra Nath: So we are still, as I said in my opening remarks on toddlers in this business. Today, we have multiple channels and these channels, depending upon the need of the customers, through multiple sources, are originating with customers for their multiple credit needs.

There are few things which we focus upon: one, turnaround time; second, meeting the credit demand subject to the credit approval process; and third, post- disbursement experience, which is in terms of timely providing all of what they wanted to do that. That is the count we don't do formal customer satisfaction service.

We have done our very large impact study, which is published on our website, and it has also multiple testimonials of what kind of impact we have created for every segment of the market. And if you read through, that would be very interesting insight in terms of very large base of 36,000 customers, what we have been able to achieve.

With respect to one aspect of further credit need or, for example, a customer which has taken a loan of machinery, loan against machinery from us, whether we have approached the customer, whether he has come back to us for taking a secure loan, that has not yet started because in terms of our installed capacity versus what we can service, there is always -- there's still a gap. But now, this year, we are gradually progressing on that as well. Then we should be able to cross-sell multiple other things which a customer needs. So it's an evolution and we are on that evolution progressively.

Moderator: We'll take our next question from the line of Tulsi Badrinath an Individual Investor.

Tulsi Badrinath: Congratulations on your excellent results. I'm curious about the experience of the branch. Out of the current branches, say about 100, how many have broken even? And when do you expect the remaining to turn profitable? Also, are you planning on expanding?

Shachindra Nath: So, we have of the 100 branches, we have roughly around 25 branches, which we call the main 25 cities in the country, which service what we call the prime customer segment. Those branches, given the size at which they operate and little higher ticket size with lower yield, most of them are broken very quickly.

So, except, I think so, five or six, which would be recent addition in this year, most of them are broken even. The micro enterprises, that's much harder business to build because these are Tier 2, Tier 3 towns and you go, these are direct originated business so you have sales, credit, collection, legal, all of that. And then you have to have an origination strategy.

You have to also build a brand, because remember, we do secured loans. So if a person who is taking a INR 10 lakh of loan, but giving the papers of a INR 20 lakh worth of his property which is his only property, right? So there is the brand establishment and recogntition has to happen.

There, we have roughly around 35-plus branches out of the pool of 71. And that's what I was saying that with every passing quarter, you will have a block of 15, 20 branches who now would keep breaking even and then they will have a positive cash flow coming to the company. So this is where we are right now.

Tulsi Badrinath: And my second question relates to GRO Score. I was just curious whether, when you can see though that between the concept and what the data actually shows you in practice, have there been some surprises or positive surprises?

Shachindra Nath: Anuj, you can take that, but I think so, this time, we have moved it to our annexures. So on the Slide 37 of our presentation, you can still see the analysis of our GRO Score and are they in line with expectation or not. We would say that they are in line with our expectations. But Anuj, do you want to add something?

Anuj Pandey: Yes. So if you recall, our GRO Score classifies the customer by risk band from A to E. And what we do continuously on quarter-on-quarter is to look at the performance, not only of our own customers, but the customers whom we have scored but not disbursed, on how they are performing on other loans which they have taken from other finances.

And so far, we find that the risk classification is stacking up quite decently, so no surprises. Although the data is still for the kind of comprehensive work which we have done, we would like to wait a little more two, three quarters more to see in case there is something else which comes in. But all the early indicators are indicating that the hypothesis of that GRO Score classification will stand good.

Tulsi Badrinath: And this is also with GRO Score 3.

Anuj Pandey: No, this is GRO Score 2.0. GRO Score 3 is what we have just piloted, that will take into account GST as well in addition to the repayment behaviour from bureau and the banking behaviour. So, that, we are going live in this quarter.

Moderator: We'll take our next question from the line of Akash Jain from Ajcon Global Services.

Akash Jain: Sir, my question is regarding cost-to-income ratio. Say for, in the presentation, it is mentioned like for FY '25 projection is around 45%. So for to reach the AUM size of around INR 20,000 crores and how will we reduce the cost-to-income ratio, like, what expenses will go off?

Shachindra Nath: So nothing would go off, only your income side would keep going up. So you have pre-invested into a physical, technological, data analytics infrastructure and your incremental cost increase in terms of the opex versus your multiplier on the AUM and asset side would keep bringing down your cost-to-income ratio.

Akash Jain: And since we are very strong on the technology front, so is there any plan to develop a special app like SBIs YONO app, similar to that kind of app for digital on-boarding of customers?

Shachindra Nath: So, watch this space. I think from mid-February you'll see it.

Moderator: We will take our next question that's from the line of Vignesh Iyer from Sequent Investments.

Vignesh Iyer: So I just wanted to know, our disbursement side is growing around like 11%, 12%, 13%. So can we expect the rate to be maintained at this, around 11% to 12% quarterly CAGR for like, at least two or three quarters going ahead?

Shachindra Nath: Sir, as I said, our disbursements are not a function that we are lowering the yield for the customer. Our disbursements are a function of our capacity, which we have built over last18 quarters, actually, right? So I don't think so that there is any decrease in our portfolio yield which will happen.

In fact, we are now working, as we see the higher yielding portfolio, microenterprises, machinery business and few others, we think that there will be few basis at least some increase which will happen on the yield. So I said this, that our opex to income ratio or our bottom line would increase by virtue of seeking portfolio and the size of the business growing a little bit of increase in our yields and opex remaining flat and in spite of probably borrowing cost going a little higher, we still think so that our profitability would keep going up from where we are.

Moderator: We'll take our next question from the line of Saikiran Pulavarthi from Pulavarthi Advisors.

Saikiran Pulavarthi: Just one quick question. You have got a very interesting slide about the...

Moderator: Mr. Pulavarthi, I'm sorry to interrupt. Sir, if you're on a hands-free mode, can you switch to handset and speak, please? We couldn't hear you clearly.

Shachindra Nath: We could hear you. You were talking about an interesting slide, yes.

Saikiran Pulavarthi: Yes. So there is a slide which explains the business model of Lending-as-a-Service where you have explained the RoAs and the RoEs, which will be far higher than normal on-balance sheet model. I do understand that you are already having certain off-book kind of a model which you're doing it.

What could be the journey from the current level, probably, to a co-lending model where we will see the RoAs and the RoEs expanding meaningfully? At what scale or what are the milestones as investors we should track? If you can just help us explain, that will be really helpful.

Shachindra Nath: So I think so that also we have given in our presentation, we have been giving it for a quite a bit of period of time. So if I may request you to look at the Slide 20. And our Slide 20, actually in fact, we were thinking of taking off this slide because we sent it, we have already explained it. So in our Slide 20, you'll see that we have said that by FY '25, the return on asset should go up to 4.5% and RoEs would go up to 17%, 18-odd percent.

And with that, off-book to on-book at roughly around 50%. Now this is dynamic. When we say an off-book AUM, this off-book AUM have multiple components, the co-lending, the direct assignment, the co-origination, so on so forth. But the broader point is between traditional and high leverage is not possible for non-bank. It's a very difficult task. If that is the constraining factor, then with low leverage to generate high returns, you have to build a semi-marketplace model, which is an off-book model. And we are a market leader, and we'll see how it evolves.

Moderator: Our next question is from the line of Rishi, a Retail Investor.

Rishi: Congratulations on a good set of numbers. I think a couple of questions that I had have already been answered with regards to what you saw this business as being different from Five Star finance and also on the gestation period of our key investors, who is been with us over four years already. So I think you've answered these questions. I just have one further question on what your official communication on the rating agency would be like. I think there was a recent downgrade on it. And I did read the announcement from U GRO but it would be good to hear from you on this.

Shachindra Nath: Exactly same thing, sir, which we have written. So we have not minced our words when it comes to what we have disclosed. So in 2019, we were signing a co-lending agreement with the State Bank of India. At that time, we had neither a requirement of any debt normally as that much of asset book and that rating was required to be taken urgently and we went to Acuite and they gave us the rating. And we signed our first co-origination agreement with State Bank of India. We didn't realize at that point of time because at that time, Acuite, which was earlier called SMERA owned by SIDBI, a large number of financial institution. This is also the same period of time where rest of the rating agencies were deeply affected by IL&FS and DHFL crisis.

So they were not doing fresh rating of fresh NBFCs, whether it was ICRA, whether it was CARE, or India Rating, all of them were deeply affected by the IL&FS crisis. So when we took Acuite rating, we didn't understand the challenge with a rating agency like Acuite. We have been raising this concern for a very long period of time in Acuite that market acceptance of Acuite is very poor.

To an extent, a large private sector bank on whose Board, there is the Chairman of Acuite is there, but still that large private sector bank don't accept Acuite rating. So having and also there is this market benchmarking, if you are used to be rated by Brickwork, Infomerics and Acuite, other rating agencies rate you one or two notch lower than those rating agencies because these Acuite and likes of rating agencies are not considered in terms of quality at par with the other rating agencies.

Acuite actually, in order to continue holding on to our business, upgraded us. First, they made us stable outlook, then they upgraded us, I think so, in August from A to A Plus. But in spite of that, we decided that we have to transition rate into larger rating agency and went ahead and took CRISIL as the rating agency. CRISIL, in all their judgement, rated us A-, which was two notch below what Acuite had rated us.

Now that is not in our control. But I think so Acuite came under severe pressure because, as you know, regulators nowadays look at it very seriously and each of the rating agency has to go and explain why their rating is too different from the other rating. And that's why when that happened, they had raised this concern that why we had gone and accepted CRISIL at a two notch below.

We told them that, look, we can't survive without with the size and scale of our operations, we cannot survive, and that's why we have taken other rating agency. And in order to self-justify themselves for a very flimsy ground which actually, if you read our letter, all of their grounds are infructuous, as in, they have no meaning, they decided to bring it down from A Plus to A.

We are transitioning Acutie out. None of our lenders, both the term lenders or any other lender have raised a single point of concern with their rating downgrade. Hopefully, this is very clear.

Rishi: And just one further question. With the funding venture that you're seeing for start-ups and other tech platforms in India, do you see any issues with the FinTechs that you are associated with on the U GRO-Xstream platform? Do you see any less participation from them in the recent past? Or anything...

Shachindra Nath: Is your question is, are we investing into those platforms? Is that the question?

Rishi: The users of our U GRO-Xstream platform where you are doing co-lending with other FinTechs like Kinara Capital, etcetera, do you see them participating less on the U GRO-Xstream platform these days or are the participation still...?

Shachindra Nath: I think so, sir, look actually, the opportunity set for that is much larger and much wider because our self-origination channel, we technically stop at that yield band of for a customer band or a risk band of what we call the 18% to 19%. There is a large set of customer population which will starts at 18%, 19% band and go all the way to 30%, 35% band.

We don't do that on our own. But obviously, there are large number of credible platforms. It can be a FinTech, it can be any small NBFC, it can be a revenue-based financing or any form of innovator, which is backed by good capital and have ability to absorb losses and is willing to work with us. So actually, the number of partnerships has our integration has gone to almost 79. However, we have been holding on to not growing that book quite rapidly.

So on an average, we are doing INR 50 crores a month. And we have been diversifying the base of our partners. We are evaluating and seeing that, should we increase this, given that now we have two years of experience, we understand each partners and there we have seen their vintage. So we right in the beginning of the next financial year, we'll take that call that whether we maintain this at the same rate where we are or we accelerate it, given the number of partners have grown.

Rishi: I have one last question, I don't know if I can squeeze it in or I can get back and move.

Shachindra Nath: Please go ahead, no problem.

Rishi: Yes, this question is I mean, I've been listening to interviews from Five Star Finance and one of the things that they said as their moat is in non-competitive nature of Tier 4, Tier 5, Tier 6, and that's why they believe that they are working off a much higher valuation than other peers. I was wondering as to how do you see this, given that U GRO is not really in Tier 4, Tier 5, Tier 6? I don't even know what Tier 6 is, to be honest, but what is, according to you, a good geographical as a speak for U GRO? How deep would you penetrate in the future?

Shachindra Nath: So I would refrain from commenting on what other players talk about their business and what their moat is, that is for the market to judge. I think so we have at the beginning of our micro enterprises channel, we think that the real credit need is in for the micro enterprises: the micro enterprises, which exists in Tier 2 and Tier 3 towns. And as you rightly said, I don't understand what is the Tier 6 town, from my experience, coming from a very small town, city, that is largely a tehsil or a taluka, very difficult for that to have a business franchise, where you can go and do too much of credit.

But Tier 2, Tier 3 town are good enough. And as per our last evaluation, we looked at the entire India and our analysis tells us that the five or seven states from a creditability perspective are the best states and roughly around 350 pin code location where the cluster behaviour of the credit is very good. So we would like to go in those five to seven states and in those 350 to 400-plus cluster locations.

Moderator: We'll take our last question from the line of Nirvana Laha, Individual Investor.

Nirvana Laha: Mr. Nath, my question is on the Lending-as-a-Service slide. So I see that earlier we used to have six banks and six NBFCs as partners. This quarter, it has come down to four NBFC. And we used to show a pipeline of potential deals, that I don't see this quarter. So my question is, to reach our INR 10,000 crores off-book target for FY '25, how are we placed in terms of these existing ten partners? And how much do we need to depend on forging new partnerships?

Shachindra Nath: So, sir, why it has come down, because we have learned the art of saying no. Because once you started with your though that actually we are a small company, we are a young company, and anyone who is showing interest, we should do all efforts and just go and sign up. We realized that in marriages, it is not just important for bride and groom to come together and tie the knot, they have to live together also and living together had different connotation. Even if you have been a boyfriend, if you have been partners and know each other for a long period of time, once you start living in the same room, it's a different story altogether.

So in view of that, certain NBFC which we signed up, but we don't think so that philosophically, our philosophies match. So we have suspended those partnerships very amicably, and we'll go back to them. In terms of why the new lines are not there, because the existing capacity we are not being able to service. The top three banks, public sector banks in India, the number which you are quoting up to 2025, 75% of that actually is among the first three banks which we have signed up, right?

And we have not been able to deliver that at all. So that's why we were under so much of pressure from existing large banks, each one of them having expectation that we will deliver INR 100 crores per month, we thought that we should limit our relationship right now and expand only next year, when so one bank has now reached up to, I think so, INR 700-odd crores, other banks has reached around INR 200-odd crores.

So I think so, INR 1,000 crores to INR 1,500 crores, wherein a large bank would pause and review us and then give us another INR 1,000 crores of line. So I think so, we have more than sufficient partnership which exists today. And at our choice, we can increase it whenever we want.

Nirvana Laha: And as an investor, if I may request not to remove Slide number 20 because every time we see the FY '25 figures, the aspirational figures, it reinforces the fact that that's what management is aiming for, and that's why we are invested. So a small request from my side.

Shachindra Nath: We will keep doing that. We expected that by giving that slide, people will not look at us from last two years perspective, and yes, they'll focus on what we are going to deliver in next two years, and they will correlate with quarter-on-quarter performance. We were not seeing any good result of that. That's why, being disheartened, we were thinking of removing it, but we'll take your input and not do that.

Moderator: I now request Mr. Shachindra Nath to add a few closing comments. Over to you, sir.

Shachindra Nath: Thank you very much for listening to us patiently and asking very good questions. Obviously, every time we come on the quarterly call and when we hear each one of you, it motivates us to keep doing what we are doing today. But even if you have further questions, Mr. Nirav Shah, our Head of Strategy and Investor Relations and his very capable team would be happy to answer you, on any further questions which you might have. We'll see you next quarter at the end of the year. Thank you very much.

Moderator: Thank you, members of the management. On behalf of UGRO Capital Limited, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.