

“Mahindra & Mahindra Financial Services Limited  
Q3 and 9M FY24 Earnings Conference Call”

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**Management:**

- Dr. Anish Shah:** Managing Director & Chief Executive Officer-M&M and Chairman
- Mr. Ramesh Iyer:** Vice Chairman and Managing Director
- Mr. Raul Rebello:** Executive Director and Managing Director and Chief Executive Officer (Designate)
- Mr. Vivek Karve:** Chief Financial Officer
- Host:** Mr. Abhijit Tibrewal – Motilal Oswal Financial Services

**Moderator:** Ladies and gentlemen, good day, and welcome to the Mahindra & Mahindra Financial Services Limited Q3 and Nine Months FY24 Earnings Conference Call hosted by Motilal Oswal Financial Services Limited. This call will be recorded, and the recording will be made public by the company pursuant to its regulatory obligations. Certain personal information, such as your name and organization may be asked during the call. If you do not wish for it to be disclosed, please immediately discontinue this 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 call, please signal an operator by pressing star, then zero on your touchtone phone.

I now hand the conference over to Mr. Abhijit Tibrewal from Motilal Oswal Financial Services. Thank you. And over to you, sir.

**Abhijit Tibrewal:** Yes. Thank you, Neerav. Good evening, everyone. Thank you very much for joining us for the Mahindra Finance call to discuss quarter three FY24 earnings. To discuss the earnings, I'm pleased to welcome Dr. Anish Shah, MD and CEO, Mahindra & Mahindra, and Chairman, Mahindra Finance; Mr. Ramesh Iyer, Vice Chairman and Managing Director; Mr. Raul Rebello, Executive Director and MD and CEO Designate; and Mr. Vivek Karve, the Chief Financial Officer, along with other members from the senior management.

I now invite Dr. Anish Shah and the senior management for their opening remarks, post which we will open the floor for a Q&A. Thank you, and over to you, Dr. Shah.

**Dr. Anish Shah:** Thank you, and good evening, everyone. It's a pleasure to have you join us for the earnings call today. I'm here in my capacity as Chairman of Mahindra Finance, just to provide a brief update on the transition of leadership before we get into the earnings numbers.

As we announced almost a year ago, we had Raul Rebello appointed as CEO and MD designate. And we had planned a very structured transition, and very happy to report that continues to go extremely well. We are now in the final phase of that. And Ramesh, who is sitting right beside me is, has now handed over the mantle of day-to-day operations to Raul and continues to provide the guidance and mentorship that Raul and the team require.

And in that construct, Raul will conduct his first earnings call independently today, with us being there, again, to provide the support and mentorship that may be needed. So that's the significant aspect of the transition. It's proceeding well. We will have Ramesh with us for one more earnings call before his retirement date, which is in April, and I'll join back again for a brief update at that point.

But before I handover to Raul, I just want to say that the business is very much on track with regard to everything that has been promised and very strong performance from an asset quality standpoint, and an overall standpoint, just progressing extremely well. So with that, I'll leave it to Raul to take you through the details. Over to you.

**Raul Rebello:**

Thank you, Anish, for those opening comments. Thank you, Motilal Oswal and Abhijit and team for hosting us today. Good evening, everyone, and yes, welcome to the Q3 earnings call. We bring you along with the senior management of Mahindra Finance here. As housekeeping, I would request you to keep the Q3 deck -- Investor Deck handy because we will be referring to the deck and I'll be noting page numbers as I refer to certain numbers.

So moving straight in into the first, page 3, actually, in your reference, which is titled as highlights for Q3. We continue to see a very strong demand momentum in the segments that we operate in and the markets that we operate in, primarily the wheels business, as you know. And Q3 always has the added festive volumes which come in.

So across banks and NBFCs, where we are amongst the top three finances, we are happy to note that we continue to maintain the leadership position in tractors, preowned vehicles, passenger vehicles and the 3-wheeler segment. We continue to have our market leadership position.

Noting the loan book growth, we are at INR97,048 crores, which is a Y-o-Y increase of 25.5%. On NIMs Q-o-Q, there's an improvement of 30 bps. We are now at 6.8%. You would have noted we were at 6.5% at the end of -- at Q2. On the asset quality side, GS3 numbers have reduced Q-on-Q from 4.3% to now 4%, which has meant that the credit cost also has had a sharp decline to 1.2% from Q2 end at 2.4%.

And if you recollect, we had guided last quarter that for the full year, we anticipate to have credit cost in the range of 1.5% to 1.7%. With Q3 numbers delivered, we believe that we are on a firm track to meet that commitment. Referring to the graph at the bottom of the slide, you would see that compared to last year, wherein Q2 and Q3, we had a very sharp reduction -- between Q2 and Q3, a sharp reduction in GS2 and GS3 by almost 210 bps, 16.4% to 14.3%.

That resulted in a very high provision release of INR343 crores. Vis-a-vis this year where GS3 has reduced from 4.3% to 4%, but overall, it's not been as sharp as last year between Q2 and Q3. So the equivalent INR343 crores provision write-back last financial year, it's only INR121 crores write-back this year, which passes to the P&L. So the overall PAT for a comparable quarter last year, we have seen a slight decline of 12%. PAT for this quarter stands at INR553 crores.

Moving to slide number 4 on your -- on the deck. Now we're providing before we go into further details of Q3, we're giving a year-to-date summary. On disbursements, we continue to have strong momentum. Cumulative disbursements of INR40,916 crores, which is a 14.4% Y-o-Y growth.

Loan book, I mentioned, is up by 25.5%. NIMs versus last year is 90 bps lower, largely by a rising cost of fund environment that we are in, and NIMs are YTD at 6.7%. Commentary on asset quality. Stage 2 is significantly lower at 240 bps lower than last year, which is at 6%. Stage 3, as I mentioned, is 190 bps lower compared to last year at 4%.

Net Stage 3, important to note, is right now at 1.5%, which is 100 bps lower than last year. So at a PPOP level, we are at INR3,005 crores, which is up 7% from last year YTD status. Provision impact, as we did mention, and I mentioned in the Q3 impact. Overall, last year because sequentially, we were climbing down on provisions every quarter. On a YTD basis, we had a

INR613 crores release last fiscal on provisions, which this year, there was a INR368 crores charge on P&L.

So it's approximately INR980 crores swing on provisions, but we have significantly lowered the settlement and disposal losses. So that number actually we have a very smaller number flowing into -- but definitely, we can't cover for the overall swing in provisions. So on a YTD basis, the PAT stands at INR1,141 crores versus INR1,300 crores for last year.

Moving to page 6, I'll -- the most in -- we mentioned numbers, we will directly move to page 6 on your -- on the deck. Overall, disbursement growth has been sequentially growing up. As you see the starting two quarters of the year were very strong. There was a low base. Last year, just to remind everyone, supply side constraints were all back to -- there were no supply side constraints. So we saw a very strong Q3 last year. And this is also a strong Q3. It's a 7% growth which means a total 14% Y-o-Y growth on disbursements. Collection efficiencies are panning out as per plan in the 95% range.

Moving to slide number 7, page 7 on your deck, which we have now attempted to give you a very product-wise update on how products have been performing. In the wheels business, you would have seen a big trend of change to SUVs, preference of SUVs has been moving up. So we have also seen an equivalent surge in our UV and SUV business, which is 21% Q-o-Q and 26% on a YTD basis. Overall, cars also has moved positively 15% Q-o-Q, 25% on a YTD basis.

The CV business has also been strong at 10% Q-o-Q and 18% on a YTD basis. Pre-owned vehicles, 8% on a Q-o-Q and 19% on a YTD basis. Tractors, as you would have heard commentary from most OEMs has de-grown YTD basis and even on the quarter. We've seen a Q-o-Q de-growth also of 18% and a 2% growth, but on a YTD basis. I would like to underline the point that we're not losing market share in the tractor business. This de-growth is very much in line with what the industry is witnessing.

Our SME business, you would have seen -- has seen a kind of a Q-on-Q de-growth and YTD de-growth. I want to underline the point here that we are moving much more to a very granular retail business in SME with LAP being the mainstay product. On the retail business, we don't see a growth. It's mostly the de-growth has happened on the Y-o-Y -- on the wholesale business. So nutshell, 7% Q-o-Q growth on disbursements and Y-o-Y 14% -- YTD -- on a YTD basis, a 14% growth in disbursements.

Moving to the next page, page 9, where we give you a trend of how M&M versus non-M&M. We continue to have M&M contribution of 45% in our share of disbursements of YTD December. Moving now to margins and spread analysis, page number 9 on your -- for your reference. As I mentioned that page number 9, yes. So you would see that income to average assets have gone up sequentially. We have started passing on pricing. So there's a 50 bps difference between the two quarters. Income to average assets at 13.1%.

Cost of funds continue to be a rising environment, 20 bps increase in cost of funds to 6.3%, so which leaves an overall NIM increment of 30 bps to 6.8%. Overheads have been range bound at

2.8% for some time now. Our write-off and provision, as I mentioned, has fallen sharply by 120 bps to 1.2%, which means ROA for the quarter is at 2.1% versus 0.9% for Q2.

Moving to the next page quickly. We have talked about GS3 numbers reducing. We want to underline here that we've had an ECL model refresh. The objective was to have a much more product-wise granularity through the ECL model. And as an outcome, we are not seeing a huge impact on provision coverage. You would see the Stage 3 has, in fact, increased by 50 bps to 62.7 from last quarter. Stage 2 has stayed constant at 11.3%.

There has been, of course, a very small release of 10 bps on Stage 1 from 0.8 to 0.7. Overall, provisioning, our requirement, we are very well covered at the INR3,655 crores, which is -- we are even sitting at a -- just go back to the previous panel. And the provision versus IRAC also, we have a cover of INR1,534 crores.

Moving now to the next page, page number 11, where we'll give you a little more granular updates on credit cost. You would see that GS3, as I mentioned, has been coming down. The breakup of credit cost here, we have been -- we've shown it two components of credit cost, provision separately and write-offs. While provision there has been a huge swing on a -- on a year-to-date basis, INR613 crores last year versus INR368 crores.

What is important to note here, the middle panel, we had a write-off of INR1,612 crores versus this year, INR1,113. This basically signifies the INR500 crores reduction in write-off, which is a very positive trend. It shows the quality of the assets and the amount of assets flowing into bad debts, which is a positive outcome for us right now. With this confidence, we are still committing to our total credit cost for the year being at a 1.5% to 1.7%.

Moving to next page, page 12. Balance sheet. From a balance sheet standpoint, the headline says it all. We are adequately capitalized. 18.3% is our overall capital adequacy. Within that, our Stage 1 is confirmed, it's at 16.5%. And coverage is at a healthy levels at 62.7%.

Now moving to page 14, wherein I'll -- this is the second last page of the slide before we move to our questions and answers. Overall, I would like to give everyone confidence that we're moving -- doing well from our overall Mission '25 delivery items. We have 1 clear strategic objective, was on asset quality, not just Stage 3 and credit cost.

When I look at the underlying sourcing mix of what's coming in through the door on New To Credit (NTC), near prime, etcetera, very healthy levels of new book sourcing. Ex-bucket opening is also at its all-time low. On digital transformation, we are on track. We have gone live with various end-to-end digital journeys on personal loans for existing customer, fixed deposits and part digital and part phygital journeys for our vehicle loans are all progressing well.

On growth through diversification, we have increased our composition of used vehicle business. Every month, every quarter, we see an increasing trend. You've noticed that used vehicle is now 17% of our origination. Our new growth engines or the SME or leasing are all also progressing well.

On the partnership side, I would say, early days, but the partnerships with SBI, Bank of Baroda with India Post, CSC and now we've added a new partner on Lendingkart for the SME business. So these partnerships are going to be key. Right now, there might be adding low volumes to our overall disbursement, but they'll be key as we go forward.

Moving to page 15 on the deck. Finally, on Mission '25 progress, I would say we are green on the first two on asset quality and AUM growth. We have been seeing asset quality, as we mentioned, is well below our stated goals. On book growth, we have been sequentially and seeing even on an annualized basis, a 25% growth.

We will, of course, calibrate our growth to keep in mind, the margin requirements that we have. On new business contribution, I mentioned, while it's a slow start, it looks like we'll be slightly below the number, aspiration number of 15% by FY25. But we have confidence in the way in which the new businesses are moving.

On the NIM side, I would like to mention that last time we have recalibrated 7.5% to 7% kind of NIM aspirations for the medium term with the way in which cost of funds have been moving. Against the 7% we have been moving decently well. On opex, 2.5% is the aspiration. We have been -- when we set this goal, we were at about 3%.

We have been moving directionally well on that front. And if all these are delivered well. ROA is an outcome metric. We are still keeping our goals on the 2.5% ROA. Directionally, I think we are moving decently well. So this is broadly a summary of where we are, a slightly longer story, but that's the summary for our Q3 numbers. I now open it up for Q&A.

**Moderator:** Thank you very much. We'll now begin the question and answer session. The first question is from the line of Mahrukh Adajania from Nuvama.

**Mahrukh Adajania:** Congratulations, Raul. So my first question is on asset quality. Do we really need a cover of 63%. Where do you see it settling in the next one to two years? And you talked about recalibration of provisions product-wise, or at least that's what I heard in the commentary. Could you elaborate, please?

**Raul Rebello:** I'll just correct, recalibration was on NIMs, which I mentioned. I think we have a stated goal of I mean we -- in our Mission '25, which we did at the end of FY22, we talked about 7.5% NIM aspiration. I said we're recalibrating that to 7%. On your first point on coverage ratio, Vivek can expand. The current coverage ratio is largely model driven. We have an ECL model, which determines the coverage ratio.

Yes, compared to peers, we would be higher. But this is a function of LGD and PD, and just looking at how things would go. We do expect this to come down by Q3 of next year. But right now, it's mostly an ECL model, which dictates the kind of provision levels that we hold in Stage 1, Stage 2 and Stage 3. Vivek?

**Vivek Karve:** I think very rightly described by Raul. So Mahrukh, there are no overlays in the provision that we maintain. So the provision number is beyond the model, which has now been further refined,

I would say at a product classification level. So that's the only change that we have done in the current quarter.

**Mahrukh Adajania:** But has that, so the write-backs that you see on provisions, that's because of refining or obviously because of recoveries?

**Vivek Karve:** It's because of refinement model.

**Mahrukh Adajania:** Okay. So what would have been any, what would have been the credit?. I mean is there a figure for comparable credit cost to September? Or it really doesn't matter?

**Vivek Karve:** No. So I think we have also talked about it in our investor presentation number. But anyway, the number is INR86 crores. So because of the model refresh, if we had not done the model refresh, the provision number would have higher by about INR86 crores.

**Raul Rebello:** Just for reference, page number 10, we have qualified the number which Vivek just underlined, underscored INR86 crores is the rupee value number.

**Mahrukh Adajania:** Okay. And my other question, again is that you said that we correct the ECL model, the rollover will correct in Q3 next year. So in Q1, Q2, you would therefore see again, high credit costs like we saw this Q1, Q2. Is that a fair assessment?

**Vivek Karve:** No, I think that is not what Raul mentioned. Your first question, Mahrukh, was on the coverage percentage, right? And you said the coverage percentage seems higher. So what we are trying to say is that the coverage percentage, we expect it to normalize at a lower level going forward. That's what we meant. We did not provide any commentary on what the credit charge will be in the first or the second quarter.

**Mahrukh Adajania:** No, no. As in the coverage will come off by Q3 is -- wasn't that said?

**Vivek Karve:** Yes, yes. So coverage, that you're right.

**Mahrukh Adajania:** That's not credit cost, okay.

**Vivek Karve:** That's what I just wanted to correct. It is about the coverage percentage.

**Ramesh Iyer:** Mahrukh, this is Ramesh here. See, the way you should look at it, is if your Stage 3 has already come down to 4%, right? And if you even maintain it at this level, there is not likely to be a very higher charge that you talked off in the first quarter will continue to have a higher charge, right? Only when the Stage 3 goes up, then you will see a new charge coming in. If they remain stated there, to the extent of the book growth happen, only to that extent, the charge will come, right? It won't otherwise happen.

And so far as the reversal is concerned, as you know, in this model, it's a 4-year history or 42 months history that we look at. And therefore, in the past, if you have had higher write-offs, that is always going to keep impacting until each year starts moving out, right? So when the book starts performing well, which has been the case in the last two years, you will start seeing the benefit of it come down, and that's the time the coverage will fall.

- Moderator:** Next question is from the line of Anuj Singla from Bank of America.
- Anuj Singla:** Congrats again, Raul. So first question is on the funding cost. We have seen a significant tightening of the liquidity and also the reset increase for bank lending to NBFCs. So Vivek, probably you can give us some outlook on how the funding outlook is there for the 4Q and the next year? And also what it implies for NIM?
- Vivek Karve:** Sure. As you rightly said, the overall liquidity environment has remained tight. However, for a company like Mahindra Finance, availability of funding hasn't been an issue given our credit rating, but the costs have remained elevated. And the -- if I were to pick up the cues both from Fed and therefore, from RBI, the regulators don't seem to be in any hurry to reduce the benchmark rates.
- So we would -- as a result, expect the incremental cost of borrowing in Q4 to remain at the same ballpark as that of Q3. And I would not like to hazard any guess on what could be the rate trajectory in the coming year because while everybody believes that the rates will come down, the timing of the rate reduction is something is anybody's guess.
- So just to summarize for you, the rates have -- are definitely higher as compared to Q2. So as a result, our cost of borrowing is higher as compared to our cost of borrowing in Q2. And we expect the Q4 levels to remain at around the same levels as Q3.
- Anuj Singla:** So unless something changes on the repo side there -- or liquidity items further. This is the kind of the peak cost of funding, which we should assume.
- Vivek Karve:** Yes, we hope to believe so.
- Anuj Singla:** Okay. Got it. And secondly, I think earlier in the call, we had mentioned that opex to asset would rise in the second half, which hasn't happened, and I think that's a great outcome. But just to understand, are the peak investments behind on the tech side? Or how do we see the trajectory on the opex to asset side from here?
- Raul Rebello:** Our attempt, Anuj, is to keep it at the same level. Investments, of course, are happening, but we have an air of being as frugal as possible and as efficient as possible. So we are maximizing on all fronts. As you know, opex is a large bucket. We will continue to make investments. We will not shy away from the digital transformation that the entire spectrum of investments that we have to make, and at the same time.
- We run a very efficient shop, a very productive shop, making sure that part of the investments we've already made are starting to show results. So we are looking at keeping this 2.8% right now. And finally, the model requires us to come down to a 2.5%. So that's how we are fashioning the business model and the number on opex to be achieved at.
- Anuj Singla:** Got it. And lastly, a more strategic question, Raul, the ROA target seems still at 2.5%, but NIM target calibrated to 7%. On the growth side, new business is lagging a bit our expectation. So what are the levers can be there for us to achieve on this 2.5% ROA target for the next year?

**Raul Rebello:** So one is, of course, that the income side also, we'd like to push it slightly higher, and we're looking at other sources of income, noninterest income sources. But largely, the other big lever is going to be credit cost if the NIMs are going to be recalibrated at 7%, let's say, opex at 2.5%. So we will definitely start making sure or not we'll definitely have to keep a much lower appetite on credit costs in the 1% to 1.5% range to get to that.

But this is, of course, going to be in a sequential manner. It's not overnight. And the good thing is that we are trending well. As you know, we have already given guidance of credit cost to be in the 1.5% to 1.7% range. But that's for end of this fiscal. Next year, we'll have to even go down below that number.

**Moderator:** Next question is from the line of Piran Engineer from CLSA India.

**Piran Engineer:** Congrats on the quarter, and congrats to Raul for the -- for your next role. A couple of questions here. Firstly, can you comment a bit on vehicle finance disbursement growth outlook? We saw a slightly tepid festive season, and it's kind of reflected in numbers in December. And I'm not just referring to Mahindra Finance, but in general for the industry. So what is your outlook? Where are the risks? Are you seeing discounts go up? We've heard that for commercial vehicles. Is that also the case for passenger vehicles. Some commentary on outlook on growth would be useful here.

**Raul Rebello:** Yes. So I'll open it up and request my colleagues also to join in. So what we're seeing definitely is break it up because they are different nuances. For passenger vehicles after a couple of years of good growth, we are seeing inventory levels at dealerships now come back to maybe two months. So we are going to see a sub-10% growth for sure going forward.

Clearly, what will provide momentum is, one, for a lender, there is a premiumization theme happening. So though the volume growth might be slightly lower, the ticket sizes are going up and SUVs are becoming now the bulk of passenger vehicles. So as a lender, even keeping the same LTVs, it gives us a benefit on overall growth. The other thing to note is most passenger vehicles, as you see now a slew of new models coming in, those models of course are creating some demand side upsides, right?

Moving to used vehicle, where we are also a participant, as the more formalization happens there, there is already a -- there's been a good increase in the amount of lending to used vehicles, which was highly underpenetrated, and we being one of the main players in used vehicle finance, we see headroom for growth there.

CV business, we are not a very large heavyweight player largely -- in M&M in the LCV, SCV segment. And now we are increasing -- in the bus segment, by the way, overall industry, you would see good growth. CV segment also decent growth. And as overall infra, mining, et cetera, goes up, I think CV has been a growth story now for two years plus, and we hope to ride that momentum.

Tractor, I would say, is in a tough spot. After two years of very high growth, we all anticipated a negative growth this year. The industry is playing out. It's been a degrowth and we don't see

with the agri the overall sowing data coming in of rabi really low, we do see a prolonged kind of stress purely in the agri segment, and that will rub off on tractor demand.

But not to say the other side of rural also -- agri might be a little down, but rural overall with remittance and overall agri, infra and those tourism, et cetera, there is otherwise slight buoyancy in the rural markets. But we would watch out for tractors. We don't anticipate a huge uptick in growth there.

3-wheelers, I didn't talk about 3-wheelers. Of course, we are the number 2 leader there. 3-wheelers has seen a 30%-plus growth. There's a huge EV change happening there. We're seeing much more movement towards EV, and we will see how we play that game too. So that's in a nutshell, I will invite Mr. Iyer or if anyone else has views on the industry.

**Vivek Karve:** And Piran, if you look at the overall growth at 7%, but if you adjust it for SME, the core vehicle finance growth is 10% for the quarter and 20% for the 9-month period.

**Piran Engineer:** Okay. So the sense I get putting the grammar into words is that disbursement growth might taper off a bit next year?

**Vivek Karve:** Yes. It is somewhere.

**Piran Engineer:** That's a fair?

**Raul Rebello:** It won't be as exuberant as what we saw in FY24 for sure. I mean one could expect FY25 to be tempered compared to FY24.

**Piran Engineer:** Got it. Got it. Secondly, we've done a good job on improving NPLs, asset quality. How should we think about, let's call it, loosely call it the revised targets for GNPL. Clearly now Stage 3, less than 6% will not be our target. Can we see it going down to, say, 2.5%, 3% like some of your peers?

**Raul Rebello:** We don't want to give any forward guidance, Piran. But yes, if we have to -- you can do the calculation, if you have to be in the 1% to 1.5% credit cost, clearly, we'll have to come down slightly more on the GS3 numbers, but more importantly, the other constituent of credit cost, which is a disposal, settlement and write-off also has to come in lower. I think at the end of Q4, we generally have a meeting in person where we give you a slightly more forward look of how we are looking at this business model. And in our next meet, you will see a little more granularity on our forward plans.

**Ramesh Iyer:** I think one important data that you may want to continuously look at is what is our Stage 2. And if that isn't growing, that's a clear indication of the Stage 3 not expected to grow any further. And as we settle those accounts, as we negotiate settle, as we repossess settle, as we collect settle, I don't see a downward trend.

**Piran Engineer:** Got it. Got it. And just my last question for Mr. Karve. Firstly, what percentage of our bank borrowings are repo-linked? And is there scope to further reduce liquidity on the balance sheet to support margin?

**Vivek Karve:** Yes. So -- not exactly repo, I would say. But I would say it is external benchmark. So yes, our floating rate is about 40% of our total borrowing today will be floating rate, which includes MCLR also. So anything which is floating and is subject to any reset is about 40%. And coming to your question on the liquidity, that recalibration continues to happen as we look at the overall liquidity and we draw comfort from the fact that flow of the pipeline needs to be decently available to us as a result of which we can take those costs to reduce our liquidity buffer. But we are conscious of the fact that excessive liquidity buffer leads to a negative carry, and we keep doing that recalibration exercise every now and then.

**Piran Engineer:** Got it. But sir, out of this 40%, can you just break it up repo versus non -- versus MCLR?

**Vivek Karve:** But we may not be able to get that granular.

**Moderator:** Next question is from the line of Shubhramshu Mishra from PhilipCapital.

**Shubhramshu Mishra:** Congratulations on the new designation, two or three questions. The first one is if we can split our employees into various functions, frontline guys, collection guys, distributor into the various businesses, and maybe some of them would be into HR function as well. The second is on the housing finance business in the fourth quarter last year, Mr. Iyer had referred to an IPO of the housing finance business three years from then.

So where are we on that? As we look at the last 50 odd quarters, the total profit pool is roughly around INR1,000 crores, which is around maybe 9% to 10% of the stand-alone profit that we made from MMFSL. So it looks like capital misallocation. So one, do you really intend to run this business in the medium term or maybe have a strategic investor coming into running the housing finance business with us?

And the third part would be, when we look at the PCR, which is roughly around 60%-odd. Now we are running a fairly secured book. So 60% in ECL would pretty much mainly LGD. So having an LGD of roughly on 60% running a majorly secured business seems out of that? Thanks.

**Raul Rebello:** Thanks, Shubhramshu I'll take the first. See, just to be fair to what we disclosed so far, on exactly number of employees in frontline, back office, et cetera. We have not yet done that. We'll probably do that and provide more granularity going forward. But to give you a sense of our large -- a large part of our organization, most of them are in business roles.

We have, for the last two years, not added any headcount in collections. We have been saying that our collections have been healthily moving towards digital mode. So we are not required to add any headcount in the last two years on collections. In fact, we released some of the collection folks into business roles and other roles.

When we look at our nomenclature tooth to tail ratio that you look at in organizations, I think we're at a healthy level of folks who hunt and do business as well as collect to back-office folks. We can, at some point of time, maybe end of Q4, where we think -- deem fit, when we give that granularity, we can give it to everybody on exactly how many headcount are in what functions. On rural housing finance, the objective right now is to bring down the GNPA numbers.

We have gone down in that effort, but there is significantly more work to be done there. I don't think we are in any mood right now to unlock value there before we get the basics in place in that business. So we continue to be committed to getting that ship in order. Mortgages is a big theme for us at the sector level.

We started doing LAP last year, but of course, we started doing it in MMFSL, but we had called out that mortgage is an important theme, and it should not be outside. It's such a big heavyweight on scheme of lending, and we will play to potential in mortgages. Rural housing finance for now the objective is to further get asset quality under control. The third question on the -- is the 63%...

**Vivek Karve:** Shubhramshu, if you are okay, because you asked many questions. If you can repeat your question on ECL.

**Ramesh Iyer:** You have a 60% coverage, does it mean your LGDs are high?

**Shubhramshu Mishra:** Yes. So on ECL essentially the Stage 3 provision coverage ballpark the LGD, right? So if we are running a fairly, largely secured book, which is asset finance we are largely asset financiers, 60% LGD seems out of whack. That's my question.

**Vivek Karve:** No, no, you're right. So I think maybe we should quickly recap as to calculate that. So your understanding is right, that the coverage would correspond to the LGD ratio. And LGD is calculated based on the past losses that we have experienced in that particular portfolio. And therefore, and Raul also made a point at the beginning of this conversation today that we have seen a reduction in our credit losses over a period of time.

So which should reflect going forward in lower LGD numbers, and which, in turn, will also reflect in lower coverages required. Also, what we should also bear in mind is the number on which this coverage is applied which is the gross Stage 3 has also been smartly coming down over the last 1.5 years.

**Shubhramshu Mishra:** So, when can we expect. As earlier, we used to have close to 35% to 40% LGD, which is roughly the PCR. When can we expect those previous levels of LGD or PCR? I know we will have a reset in the fourth quarter, we have already done that. But irrespective of the reset, when do we see that level of PCR?

**Vivek Karve:** No. So we may not be able to give you an exact guidance. However, responding to the first question that was asked today, we are expecting some stabilization of LGD in the next fiscal.

**Shubhramshu Mishra:** But it won't come down to 35%, 40%?

**Vivek Karve:** I cannot say, yes, I cannot say no because then I'm almost giving you a guidance. But what I can only say is that we are expecting normalization to happen.

**Moderator:** Next question is from the line of Viral Shah from IIFL Securities.

**Viral Shah:** Congrats on a good set of numbers. I had a few questions. So one is, first of all, Vivek, you mentioned about the cost of funds. So you were referring to the incremental cost of funds. Can

you quantify what is the incremental cost of funds given your back book cost of funds seems to be around 7.8%.

**Vivek Karve:** Yes. So you are right, the overall cost of funds is about 7.8%. And therefore, the incremental cost of funds is in the ballpark of about 8%.

**Viral Shah:** So basically, as this kind of reprices, there is some bit of further increase in cost of funds that can happen?

**Vivek Karve:** So what I mentioned is that in the immediate future, we are expecting this cost of the -- incremental cost of fund to remain in the ballpark of what we have experienced in the third quarter. Very difficult to exactly estimate that number because the situation is very dynamic.

**Viral Shah:** Right. Fair enough. I understand. The second thing is on the yields. So over there, of course, there was an unwinding of the trade advances, which was there. Apart from that, what was the major driver for the yield expansion of 45 basis points quarter-on-quarter?

**Raul Rebello:** So see, it takes time to transport at a book level, but we've been seeing a steady increase in our fee-based income, which we have been for a while driving now. So we -- in the festive season very rarely, do you become very sharp in transmitting rates or increasing rates. I would say most of this benefit has come from the fee-based income, which we -- which we've started to unlock. Unlock incremental revenue from it.

**Vivek Karve:** And in this quarter, we increased the rate by some 20-odd basis.

**Raul Rebello:** So that's besides the rate increase. We took a marginal rate hike, but now we'll pass it on mostly.

**Viral Shah:** And can you quantify what proportion of your book is now repriced to the higher rate in terms of reflecting on the P&L?

**Vivek Karve:** No, we may not be able to disclose that number. When you say repriced, what do you mean by that?

**Viral Shah:** So basically, the share of the higher rate book. So that would be the pre FY22 book, which will be there and its share will be coming down. But do you have any numbers which are there if you can let us know.

**Vivek Karve:** Yes. Frankly, we don't go that granular.

**Viral Shah:** Okay. Fair enough. And the last question I had was in terms of the branch expansion. So in last three years, there is no major branch addition that has happened. And going ahead, I see in your PPT that you have guided for around 100, 150 odd branches to be added in the next 1, 1.5 years. Your opex guidance take that into account?

**Raul Rebello:** Yes. Whatever we have -- I mean the opex guidance of 2.5% by end of FY25, now that's an aggressive number. But overall, when you look at -- and this will be a phased plan of rollout of branches. And you're right, we haven't opened branches in the last two years because we were, of course, remodelling the branch structure, et cetera. And now you will see us opening more

branches as part of our overall distribution and growth plans, but the number of branch and the amount and the cost associated is overall baked into our opex assumption.

- Viral Shah:** And congratulations, Raul, on the job ahead.
- Moderator:** Next question is from the line of Shweta Daptardar from Elara Capital Plc.
- Shweta Daptardar:** Congratulations. A couple of questions. So you mentioned on cost of funds from bank borrowings. So am I very much right, so 60% are not EBLR linked and sort of -- so you mentioned 40% are EBLR linked and the entire portfolio is floating.
- Vivek Karve:** No. I think that's not the correct understanding. In fact -- because we deal in vehicle finance, the vehicle finance loans are typically fixed rate loans. So therefore...
- Shweta Daptardar:** I'm sorry, I'm interrupting you, I'm talking about bank borrowings?
- Vivek Karve:** Yes, yes. So what -- yes. So when we say 40 -- in fact, the correct number is 46%. So 46% of the total borrowing is floating, which means 54% is fixed.
- Shweta Daptardar:** And what could be incremental cost of...
- Vivek Karve:** Let me also correct. It is not just bank. When I give the number of 46%, it is of the total outstanding borrowings that we have.
- Shweta Daptardar:** Okay. What is the incremental cost of funds on bank borrowings per se?
- Vivek Karve:** I'm sorry, but I will not be able to give you such a granular answer.
- Shweta Daptardar:** Sure. Sir, secondly, on the disbursement funds so year-on-year basis, there has been a drop of as high 30% in personal loans from consumer loans. Apparently, of course, the entire industry is wary about this particular segment. So what is your read through here and general feedback?
- Raul Rebello:** See, we were doing personal and consumer durable loans, largely on a pilot basis. Very frankly, we have actually, in December, taken a call to pause consumer durable loans. We realized there is a crowding in the market, and as a late entrant, the entry barriers are too high. So we have actually sunset our consumer durable aspirations, and we're not going forward. On the personal loan side, as you know, it's -- we're doing it only on existing to our customer base. And considering we are still in the early phase of development, refining our scorecards, we are in that learning curve. And once we have full conviction, we will amplify the monthly throughput numbers.
- Shweta Daptardar:** Sure. Sir, second bit is taking it further. So you had mentioned on the previous call that you'll be focusing more on prime customer base across certain key products. So would you like to give a fair color on the same now?
- Raul Rebello:** Without getting into specifics, when we talk about prime customers, as you know, we have a fair share of new to credit customers, prime and close to prime customers. Our proportion of new to credit overall, is coming down. But today, even in new to credit, there are various layers

of new to credit. There are scores, even our internal scores also are able to grade new to credit customers where we are focusing on those customers where we have more insights on and who have historically as per our score card had a lower sloping of risk.

So in the overall new to credit, cohort has come down. We have -- in our origination volumes, we are seeing more prime and close to prime customers. And subprime customers as a cohort also has significantly come down. Now what's driving this, as you know, in the passenger vehicle segment, there's a premiumization happening.

So by default, the demand is coming in also from customers, the prime segment customers. And we are conscious what should be that ideal product mix because we have to also protect for margins. And we are playing to that overall volume to price ratio that we expect to build into the business model.

**Shweta Daptardar:** Understood. And sir, one just last question. Collection efficiencies have been dwindling, and the cumulative numbers have been below the previous year. So how do you read into this?

**Raul Rebello:** So I don't know what -- if you refer to the slide on collection efficiency, we have been range bound. As you know, quarter three has a lot of festive period numbers. But -- that's why it's probably slightly lower than quarter two. But if you look at it on comparable basis, Q3 of this year versus Q3 of last year...

**Moderator:** Participants please stay connected. The line for the management dropped. Ladies and gentlemen please stay connected while we reach on the management back to the call. Ladies and gentlemen thank you for your patience. We have the line for the management be connect. Sir, you may go ahead.

**Raul Rebello:** Yes. Sorry, we dropped out while we were expanding on the explanation of collection efficiency. The question was whether our collection efficiency is falling, and we were just underlying the point that refer to slide number 6. We have been in the same range. It might have sequentially fallen down by about 100 bps from 96% to 95% for Q2 versus Q3.

But there are seasonality's, minor months of slight movement of collection efficiency. But overall, we are in a positive and a decent range of 95% for the whole year versus again, 95% for last year. And if you look at Q3 of last year, we were again at 95% versus Q3 of this year at 95%.

**Moderator:** The next question is from the line of Kunal Shah from Citigroup.

**Kunal Shah:** Yes. Congratulations for a good set of numbers. Firstly, with respect to the trade advances on lending and the benefit on the yield because we see that cost of funds have gone up by 20 basis points, but still new expansion is 30. So what has led to this yield improvement actually?

**Raul Rebello:** Yes. So Kunal, we did clarify. Yes, Q2 usually sees a bump up in terms of trade advance, which is not income accretive, and that part gets released into retail conversion. So there would be some benefit in the yield in Q3 over Q2 on that front. But we are also seeing a sequential increase

in our other sources of income, which we have for some time now been making investments on those other sources of income, which has started to now add to the overall income level.

**Kunal Shah:** So this would be largely sustainable?

**Raul Rebello:** I'm sorry?

**Kunal Shah:** This would be sustainable?

**Raul Rebello:** Yes, they would be -- I mean, I don't think they would be lumpy in nature. These are other income items, which we plan to sustain over a period of time. And in fact, grow further.

**Kunal Shah:** Sure. And secondly, on the borrowing side, so you mentioned not seeing much increase in the rates. So is it like larger part of our bank borrowing gets classified as PSL. And that's the reason post the risk weight increase also we will not see any kind of a pass on from the bank side in terms of the higher rates?

**Vivek Karve:** No, Kunal, that's not true. Not the entire bank borrowing for us will be PSL linked. So to that extent, there will be some pressure from the banks wherein banks will push for a rate hike. And we are not an exception, as you would have heard in other conference calls also. But we will always try to mitigate that impact either through the negotiations with the bank or by maximizing our PSL.

**Kunal Shah:** Okay. Okay. And if I can squeeze in one last question, particularly on the overall consistency in the asset quality, I think post Q4. Dr. Anish Shah: and all of you highlighted that, that's going to be the key objective. We still saw the volatility this year where in first half it was high, maybe this quarter, we again saw an improvement and Q4 is generally better.

But otherwise, when should we ideally see now with these levels of Stage 2, Stage 3 and all the efforts which are being put in, plus moving -- slightly moving towards the prime customer base. When should we actually start seeing the more stable asset quality and the credit cost outlook or maybe that's more annual and quarterly volatility will still continue?

**Raul Rebello:** So Kunal, I'll take that. I think, if you look at post FY22, there's been clearly a decline in at least the two key metrics of GS3 and credit cost. We did qualify that last quarter, the bump we saw was typical to 1 product, which was mostly the tractor business because of -- there were unseasonal rains and there was an impact on cash flows.

We are in the business. We are in rural, we are working with a large cohort of self-employed customers. But with the controllable influences of how we can reduce the volatility in that segment, with good underwriting, good collections, I think we have covered a reasonable distance.

And just from the fact that the last seven, eight quarters have seen a secular decline in those numbers, we think there should be inherent confidence that you take away from the normalization of volatility in the numbers, the full volatility will completely go away. There will

be -- for this underlying segment, there are variables in our control, which we are optimizing on and we'll continue to.

**Moderator:** Kunal Shah., I request you to come back in the question queue for a follow-up question. Next question is from the line of Umang Shah from Kotak Mutual Fund.

**Umang Shah:** Congratulations on the quarter. I just have one question, which is related to the point that Kunal was making. Clearly, in last two to three years, there are a lot of actions which have been taken by the management. Some of them we would like to believe are more structural in nature, and some benefits you would have got because of the tailwinds in the economy.

I just want to understand that, see, you might in the year sub-4% gross Stage 3 number, right? I mean, clearly, that is something which -- I mean we are seeing lower NPA numbers for Mahindra Finance only in the previous NPA recognition regime, right, which was relatively more liberal.

So clearly, there will be some mean reversion. The only thing -- I'm not looking for a number, but how confident is the management that when the mean reversion happens, it is not as sharp as that we have seen in the past, thanks to some of the structural changes that we would have taken to control this asset quality volatility?

**Raul Rebello:** Yes. So a very relevant question. We should acknowledge we are in a slightly benign environment. We have mentioned in previous calls that -- and you've said it yourself structural changes and structural initiatives and investments have been done. From an origination standpoint because we do believe asset quality is a function of both underwriting, onboarding as well as collection efficiency. We have mentioned in the long tail of earn and pay customers.

We have steadily decreased the most volatile cohort in that segment. We have, in fact, given up 5% to 7% of what we have qualified from the learning's of two crisis. One is demon and the second being COVID, we have actively in various cohorts of customers in different vehicle categories, reduced participation in that what we have localized and seen as extremely high volatile customer segments.

And in the next downturn, whenever that happens and if it happens, we do believe we'll be in a much better place considering we have taken those structural calls. Also within the self-employed customer, new-to-credit customer segments, our overall engagement with that customer segment as well as our high touch with both physical, phygital and digital, making them conscious about credit culture of keeping credit bureau scores healthy.

We've been partnering with our customer segment in a very structured manner to make sure that in times of stress we will not face the kind of swings we have faced in the past.

**Ramesh Iyer:** I think just 1 way to look at it as fairly fall over a period from Stage 3 actually has moved to Stage 1. If you look at our Stage 1 now, between Stage 2 and Stage 3, together, it's only 10%. So therefore, 90% is in Stage 1. So that reflects the actions that have been put in place and that's reflected in the asset quality by looking at the Stage 1.

**Moderator:** Thank you. Next question is from the line of Harshvardhan Agrawal from Bandhan Asset Management.

**Harshvardhan Agrawal:** I just wanted to understand on this refinement of the ECL model that we've done. Is this a onetime exercise or is it repetitive exercise that we undertake and what is the frequency of it? So the idea to understand is this INR85 crores benefit that we have got, can that reoccur? And what could be the frequency of that?

**Vivek Karve:** Yes. So the exercise -- the benefit that we have got is incidental to the refresh. So let me just clarify that first of all. And the refresh that we have carried out, we believe, is to recognize the fact that over the last four to five years, ever since we had created that model for the first time when we first came in, the portfolio has grown and each of the product -- individual product portfolios by themselves have grown.

And therefore, they carry their own risk and reward metric, which was important for us to recognize in the whole design of ECL. That's the reason that we have done this -- we have done this refresh. And on an annual basis, we will keep looking at this model. We will keep refreshing the -- reviewing the model and refresh, if required. But the -- your question on benefit or no benefit, I think that's an incidental outcome of the refresh that we have done.

**Harshvardhan Agrawal:** So sir, just to understand this annual refresh is done in every 3Q or like say next year, we'll do the refresh in 3Q once again. Is that a correct understanding?

**Vivek Karve:** You can say that, yes.

**Moderator:** Next question is from the line of Nischint Chawathe from Kotak Securities.

**Nischint Chawathe:** Just two questions. One is, what is the GNPL as per RBI norms?

**Vivek Karve:** So it's about 5.5%.

**Nischint Chawathe:** 5.5%. Okay, 4% versus 5.5%. Okay. The other is on the SME loans. Raul, you kind of mentioned that you're moving from larger tickets to smaller tickets. Maybe if you could just elaborate that what exactly is the change in strategy and what's driving it?

**Raul Rebello:** Yes. So the way we -- see our SME plays largely into -- in the retail segment, we call it as LAP and business loans. And in the slightly higher tickets, basically, we do business enterprise loans. So the differentiation is enterprises with INR25 crores and below turnover and above INR25 crores. So the focus right now is enterprises with a turnover less than INR25 crores. And largely, the incremental business that's happening there is through LAP, right?

Machinery loans, we continue to do because we've been doing it for a period of time, and we've had pretty good credit costs as well as growth outcomes. What we continue to do in the -- in the slightly larger ticket is because we have quite a few of the vendors to the M&M group supplying both to the farm as well as the auto sector. We do a bill discounting.

We have been doing it for some time now, and we're getting more traction there. Of course, that's a business which is not as competitive as the retail business in terms of NIMs and ROA,

but we do it because it's a very secure business and there's hardly any opex in that business. But what we've really seen going forward and what we have taken a call is you really can't amplify LAP business.

It's a very structured business. You've got to have deep distribution both within the organization as well as with DSAs and the DSA community. We've had a new LAP head who has joined us three months back, who was running LAP at scale in a different organization. And as he is building out this team, we've also built out the whole underwriting team for LAP. It's carved out as a very separate SBU.

There's a separate FCU unit for LAP and there is a separate underwriting, as I mentioned, and a separate collection vertical. So a new collection head for LAP, a new business head for LAP and an FCU unit is the additions they've all done in Q2 of this fiscal, and we do see that business growing stronger as we go forward.

**Nischint Chawathe:** And the specific reason why you would have probably kind of gone slow on the larger ticket LAP is because of yields or credit costs?

**Raul Rebello:** Mostly yields, and these were also business enterprise loans to -- as you say, in the MSME segment. Our focus now is on the micro small. Medium, we believe, is becoming very -- the barriers to play there with banks becoming very aggressive pricing-wise. So we largely to read it, we are giving up on the medium enterprises, which are above INR25 crores where we would give short-term loans or term loans. That's why we are kind of scaling down on.

**Nischint Chawathe:** And sort of -- sorry, just stretching this further. Can we sort of then read that this is kind of moving a little bit away from prime? I mean, is that right way of looking at it?

**Raul Rebello:** Not really. I think in the [INR25 crores to INR1 crores] LAP business, we will get a decent of close to prime and prime customers.

**Moderator:** Ladies and gentlemen, we will take that as the last question. I'll now hand the conference over to the management for closing comments.

**Ramesh Iyer:** Hi, everyone. So I think true to our belief, the customers, we always felt as things improve on the ground, we would see them perform in a way very different from when the things are difficult. And that's been reflected in our numbers quarter-over-quarter. And they have shown their resilience and they have been able to repay very, very regularly.

And we always said that these are not intentional defaulters, they are the circumstantial ones, which normally delayed and we are seeing that. I think also important to note that while we have learned through that, we have also added new segments to the business. And those customer profiles are allowing us to be more stable in terms of our asset quality is concerned.

And you will see, therefore, over a period of time, how the Stage 3 numbers stay at the lower end, and even in the most disruptive situations, they don't jump back to higher numbers. And those are purely by selection of customers, the underwriting standards that have been put in and

giving up of certain segments that were very volatile in nature. I think those are the steps that have been clearly taken.

I think what has also been proved by this model over a period of time that amidst all competition out there, I think there is a significant advantage to a model and a player who've been there for very long, have built large relationship with the dealers community, which continue to be the source of business provider as well as a company with large customer base, their ability to retain customer and self-generate a lot of business.

Even if you look at our numbers today, at least about 15%-odd or maybe upward of 15%, close to 20% is self-generated business and that is going to remain a big strategic differentiator when it comes to playing with the competition out there. I think it's important to also note that while the loans are fixed rate, as the borrowing cost starts to come down, over a period, we would get the benefit of NIMs.

While we're not able to put a number to it today and a time to it today, but we have historically seen that clearly when the borrowing cost goes up and when our liability corrects, that cost has to be borne by us, which we have seen in the recent past. A similar reverse benefit will be seen when the borrowing cost starts to come down and we change our borrowing profile, we'll start getting the benefit, and you will see the reflection of that in the NIMs while we are not able to put a number and a date to it at this stage.

We continue to believe that the rural market continues to be positive in sentiment. And as we have discussed several times in the past, the cash flows which drive this, are the tourism cash flow, the people movement overall, the infrastructure cash flow and the farm cash flow. Well, there has been some talk about the lowering of the farm output, but I personally think that the support prices would be adequate to cover up for the yield drop, if any.

And therefore, the three cash flows or the four cash flows on which rural depends continue to remain positive, and that's reflected in the overall disbursement growth that we are witnessing, and we would continue to see that. I think our investments will continue in the area of branch expansion. It will continue in the area of technology -- investments in technology and data as well as in people and people capability development.

Because while they do bring some temporary pressures on the P&L and opex will stay a high temporarily, but they have disproportionate benefit when you look at a 3-year kind of a period horizon and therefore, we would not shy away from that. And putting all of this together, we very strongly believe that the commitment that we have made for 2025 are definitely an achievable commitment from our side.

And I think every effort is in that direction, and you have seen it quarter-over-quarter that numbers reflecting in that particular direction. Particularly what gives us absolute comfort, confidence and happiness is the growing of Stage 1 and coming down of the Stage 2 and Stage 3. I think I've emphasized this even in some of the answers before, and it's super important to therefore, understand that if Stage 1 remains that high, under any volatile condition, they don't inch towards becoming an NPA.

And second is the bad debts coming down and termination going up is again a positive trend, which means we are able to reach out with this customer, negotiate and settle with. So if you kind of look at both of this, and overall, therefore, termination and bad debts come down in a manner and Stage 1 goes up in a manner, I think, the promise of returns that we are talking of would be very visible as we see quarter-over-quarter.

And we are conscious of the fact that even if we have to give up some business at the cost of not able to be completely confident of certain quality, we are more than willing to do that. At this stage, we have tightened all norms around it and therefore, the overall confidence of growth with asset quality focus and return in mind. I think that's what we are seeing in rural and the semi-urban and a little of what we've started doing as a prime customer, the three together allow us to do that.

So I would stop there with that to confirm to you that the trends that we see are here to stay, and we would seek improvement on a continuous basis. Thank you for joining this call and thank you to the organizers.

**Vivek Karve:** And thank you for hosting us today, Abhijit.

**Raul Rebello:** Thank you, Abhijit.

**Moderator:** Thank you very much. On behalf of Motilal Oswal Financial Services Limited, that concludes this conference. Thank you for joining us. You may now disconnect your lines. Thank you.