FIVE STAR
Business Finance Limited

Date: May 16, 2023

The National Stock Exchange of India Limited,
Exchange Plaza,
Bandra-Kurla Complex,
Bandra (E), Mumbai 400 051
Symbol: FIVESTAR

BSE Limited
Listing department,
First floor, PJ Towers,
Dalal Street, Fort Mumbai 400 001
Scrip code: 543663

Sub: Transcript of the Earnings Conference Call for the fourth quarter and financial year ended March 31, 2023

Dear Sir/ Madam

Pursuant to Regulation 30 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, please find enclosed the transcript of the Earnings Conference Call held on Wednesday, May 10, 2023

The transcript can also be accessed from the link: https://fivestargroup.in/investors/

Kindly take the above on record.

For Five-Star Business Finance Limited

BASKARAN SHALINI

Digitally signed by BASKARAN SHALINI
Date: 2023.05.16 18:40:03 +05'30'

Shalini Baskaran
Company Secretary & Compliance Officer

"Five-Star Business Finance Limited

Q4 FY '23 Earnings Conference Call"

May 10, 2023

MANAGEMENT: **MR LAKSHMIPATHY DEENADAYALAN – CHAIRMAN AND MANAGING DIRECTOR – FIVE-STAR BUSINESS FINANCE LIMITED**
MR RANGARAJAN KRISHNAN – CHIEF EXECUTIVE OFFICER – FIVE-STAR BUSINESS FINANCE LIMITED
MR SRIKANTH GOPALAKRISHNAN – CHIEF FINANCIAL OFFICER – FIVE-STAR BUSINESS FINANCE LIMITED

MODERATOR: **MS MAHRUKH ADAJANIA – NUVAMA INSTITUTIONAL EQUITIES**

Moderator: Ladies and gentlemen, good day, and welcome to Five-Star Business Finance Limited Q4 FY '23 Earnings Conference Call hosted by Nuvama Institutional Equities. 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 this conference call, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Ms. Mahrukh Adajania from Nuvama Institutional Equities. Thank you, and over to you, Ms. Adajania.

Mahrukh Adajania: Yes. Hi, good morning, everyone. I welcome you all to the Five-Star Business Earnings Call for the Fourth Quarter and for the Full Year FY '23. We have with us the top management team of Five-Star. I welcome them. We have the CMD, Mr. Lakshmipathy Deenadayalan with us; CEO, Mr. Rangarajan Krishnan; and CFO, Mr. Srikanth Gopalakrishnan. Congratulations, sir, on a very strong set of numbers, and I now hand over the call to the Five-Star team. Thank you, sir.

Lakshmipathy Deenadayalan: Yes. Thank you, Mahrukh. Good morning, all. Again, a warm welcome to the fourth quarter results and the third conference call that we are taking post-listing. Just to recap what I was talking about Five-Star and its business model for last two calls, Five-Star is into a niche segment where the challenges and the competitors are low. We cater to lending to an unlent segment, broadly to single and small shopkeepers, self-employed, and the cash salary segments of this country; where we see a lot of opportunity and the edge what Five-Star has of 20 years of lending to them and the collection model that what we have set up exactly suits to the earn and pay customers.

Now, getting into the quarter's number. As I said last call that the next Q4 will be the beating the best. Yes, both from a collection's perspective, from a growth perspective, we have beaten our best i.e during COVID numbers and even previous to COVID numbers. Just to take you through on the numbers, going from the branch expansion, which is the first lever of growth for Five-Star, we have added close to 73 branches for the full year. We have moved from 300 branches to 373 branches as of 31 March. And we have also added the employee strength. What the second lever of growth will come from feet on street, we have moved our employees from 5,675 to 7,347 employees, adding 1,600 employees for this full year.

That has resulted in a good disbursement. Between last quarter and this quarter, we have moved from INR910 crores disbursement to INR1,110 crores of disbursement, which is 22% quarter-on-quarter growth. And for the full year, we have increased our disbursement from INR1,756 crores to INR3,391crores, which has resulted in 93% increase in disbursement. And the outcome of branch addition, employee addition and increase in disbursement, the AUM has grown very well. Between last quarter and this quarter, the AUM has grown from INR6,242 crores to INR6,915 crores with a double-digit growth of 11% in a quarter. And for the full year, we have moved from INR5,067 crores to INR6,915 crores, registering a 37% full year growth.

And moving to the asset quality, which is the outcome of the risk, collections, what I said earlier, let me take you to a 90+. Our 90+ in last quarter was 1.16%, that has dropped down 12 bps to 1.04%. And the NPA terminology, which has changed under the revised RBI guidelines, also has seen a reduction from 1.45% last quarter to 1.36% this quarter with a drop of 9 bps. So to conclude, 90+ is

1.04% and NPA is 1.36%. The difference of 0.32%, which is INR 22.12 crores of loans, has been tagged as NPA under new revised guidelines even though they fall under less than 90+ DPD.

Translating a good collection, now let me take you through the profitability. Our profits also seen a good rise both quarter-on-quarter and for the full year. On the quarter-on-quarter, our profits have risen from INR151 crores to INR169 crores, registering a 12% growth. And for the full year, we have moved our PAT from INR454 crores to INR604 crores, registering a 33%. And both from a good asset performance, even from the liability side, we have performed very well. Our borrowing from last quarter to this quarter, incremental borrowing has moved from 9.1% to 9.5%. We are borrowing slightly little costlier from 9.1%, we have moved to 9.5% this quarter. This is incremental borrowing. But cost of fund in the book has dropped down from 10.5% to 10.1%. So still, even RBI has increased the repo rate by 250 bps, still we are able to get at a very attractive borrowing from the banks due to as we said, due to our performance, quality, profitability and good capital what we have.

So with this, let me hold myself and hand over to Srikanth for more details.

Srikanth Gopalakrishnan: Very good morning to all of you. At the cost of a few repetitions, please bear with me, but I'll just give you a quick overview in terms of how the quarter and the year went by before opening out for questions from you. Like Mr. Pathy said, I think one of the other key metrics that we delivered during this year is we almost got close to a loan base of about 300,000, representing a 25% year-on-year increase from about 215,000 to about 300,000, as we speak. The strong branch additions of 73 resulted in a disbursal increase of 93% for the year. For the quarter, we disbursed a little over INR1,100 crores. The AUM has grown by about 37% from INR5,067 crores to INR6,915 crores.

For the financial year, I think from a financial metrics perspective, the average yields have been pretty much stable at around 24.2%. The average cost of funds is at 10.12% resulting in a spread of 14.11% as against a spread of 13.5% for FY '22. The NIMs also have seen an increase. It has improved about to 18.04% as compared to 15.09% for the full year FY '22. Our cost-to-income continues to be around the 35%, 36% levels.

For the financial year 2023, it was at about 36.4% as compared to 36.92% for FY '22. All this has resulted in a healthy return on assets of about 8.62% for the full year and ROE of 15.03%, but more importantly, I think the ROA for the quarter was again at 8.62% and ROE at 16.1%, which gives you the direction of the ROE trajectory in the quarters to come. So the ROE has been going up quarter-on-quarter.

From a borrowing profile, I think we have a very well diversified borrowing profile of about 50 lenders lending to us. Banks contribute about 56% of our debt. We have also issued NCDs. We have done securitization transactions and also done an issuance of external commercial borrowing. During the quarter, we raised over INR1,400 crores of incremental debt at an all-in cost of about 9.5%. For the full year, our liability increase has been at about INR3,100 crores of incremental debt at an all-in cost of about 9.2%.

While the incremental costs went up by about 40 basis points compared to the previous quarter, as alluded by Mr. Pathy, but we are still borrowing a very good quantum of debt at optimal cost. And our cost for the full year as compared to the last year has actually gone up only by about 42 basis points. But during this period, we have seen RBI raised the repo by almost 2.5%. So that's a very strong performance from the company side in terms of the liabilities.

During the quarter, ICRA, our existing rating agency, also upgraded our rating to AA-. We are hoping that the other rating agency would also follow it shortly. The on-balance sheet liquidity continues to be extremely robust. We are sitting on a liquidity of over INR1,600 crores as of March 2023. So this is something that can actually help meet our growth targets for the next couple of quarters. Collection efficiencies have shown a significant improvement. It stood at 100.5% for the quarter of March 23.

More importantly, from a trend perspective, I think for the last 5 quarters, we've actually been clocking collection efficiency of over 100% every quarter with the exception of June '22 quarter. Even there, we were very close to 100%. And this has resulted in our buckets also becoming better. Our 30+ has been showing a consistent improvement over the last few quarters. And as of March '23, we had 30+ of 10.5%.

I just want to impress upon one fact that this decrease has not just come in percentage terms, but every bucket has actually shown improvement in absolute terms as compared to the previous quarter. So the 1 to 30, 31 to 60, and 61 to 90 has actually shown an absolute improvement. In terms of the revised upgradation norms, the revised IRAC circular, our NPA, which was at 1.45% last quarter, dropped to 1.36%. The 90+ stood at 1.04%. This also came down by about 12 basis points as compared to the last quarter. Our provision coverage continues to be robust. On the Stage 3 assets, we are holding a provision coverage of 49.33% and overall provision coverage of about 1.61% on the overall AUM.

So with the effects of COVID completely receding and good improvements seen across our portfolio buckets, we are very confident that our PCR on the overall AUM will start normalizing in the coming quarters. On the restructured book, this number has come down. What was 1% last quarter has actually come down to about 0.86% of our overall loans in the restructured book. And even on this portfolio, we maintain a provision coverage of about 59.18%, and the restructured assets have actually seen repayment behaviour of 1.5 years post moratorium that we gave. And even today, 91% of this restructured book continues to be in the standard category with only 9% slipping into NPAs.

The year-on-year profitability rose from INR117 crores to INR169 crores and increase from INR151 crores to INR169 crores profitability for the quarter. For the full year, we have shown a 33% increase in profit going up from INR454 crores to INR604 crores. Our net worth stood at INR4,340 crores as of 31, March 2023. So with the growth momentum fully back, the collections and asset quality remaining extremely robust, not just in this quarter but over the last 5 to 6 quarters. I think we believe that we remain extremely well poised to take advantage of the huge opportunity available in this segment. So that's a synopsis of the quarter and the year for you.

We will now take any questions that any of you may have. Thank you.

Moderator: The first question is from the line of Pranav Mehta from Value Quest Investments. Please go ahead.

Pranav Mehta: Congratulations, sir, for an excellent set of numbers. So first question is on the liability side. So you did touch upon it briefly in your opening remarks, but I would like to know more from you about the steps that we have planned for the next year to basically granularize and further diversify our sources of borrowing, given that our liability requirements will be significant to fund our growth aspirations. And whether the average cost of funds, we should expect to continue trending downwards. So that is the first question.

And secondly, if we look at the P&L, the fee income line, so far this quarter as well as for the full year, there has actually been a significant drop in this line item. So if you can just explain what has led to this? These are my two questions. Thank you.

Srikanth Gopalakrishnan: So Pranav, taking the liability side first. What is important to note is that whatever borrowings that we have, the INR4,200 crores have not come in from a small set of lenders. It is actually coming from about 50 lenders for us, and this includes the largest of the public sector banks, the largest of the private sector banks, who have only a small exposure with the company. So even the likes of, let's say, a State Bank of India has about INR500 crores of exposure in the company, which is not even 10% of the overall asset base. So there is a significant headroom available for us to increase our borrowings from all these people.

And from a structure perspective, we are -- we have the expertise to borrow through term loans. We have the expertise to issue nonconvertible debentures. We have done securitization transactions. In fact, in the last quarter, we did almost about INR600 crores of securitization. We did the largest transaction of about INR350 crores with DBS Bank. And so today, banks are also actively looking at taking securitization exposures. So we are very confident that even if we are able to push this -- the exposure limits to 2x with each of these lenders, we will be ending up with almost INR8,000 crores, INR8,500 crores of liability book, which is sufficient for the growth that we are looking at for next year.

So we are not really looking at any challenges on the liability front. See, from a rate perspective, our belief is we have probably seen the tip of the curve. It is probably going to stabilize at this point. Maybe not for the next couple of quarters, we will see easing coming through. But maybe towards the later part of the year, we could see some easing. But we are not seeing any incremental increases to come from here. So we should be borrowing at around the 9.50% to 9.75% levels that we are borrowing even in Q4. With the book cost at around 10.1%, any borrowing less than 10.1% mathematically will only give us a benefit in terms of the cost of funding on the book going down or at least staying at 10.1%. So both from a quantum perspective and from a cost perspective, we are not actually seeing any impact to come in, in the current financial year.

Moving over to your question on the fee and other income. See, this is purely from the perspective of an accounting treatment difference, Pranav. Earlier, the -- see, we used to collect INR2,000 at the time of log-in to ensure that the customer is actually serious about onboarding the loan. In the past, what we used to do is this used to be completely recognized in the top line. But as per IndAS this is supposed to be treated on an amortized cost basis. You'll have to knock off whatever direct expenses for origination that the company incurs, and only the balance can go into the top line, that too on an accrual basis.

So if you look at it, whatever legal -- the initial legal and inspection fees that we collected, about 80%, 82% of that gets knocked off against the expenses. Only 18% goes to the top line. That is where you're seeing a drop in fee income from about INR32 crores to INR22 crores for the current year. Despite the fact that the disbursals have been significantly more robust as compared to the prior year.

Lakshmipathy Deenadayalan: So Pranav, to the -- to add one point to what Srikanth said on the first question, on liability side, see our rating has moved from A to AA in the second, third quarter of last financial year. That is not fully capitalized. So we will expect the further big names to come in and quantum's and that will also push down the pricing to the extent what we can bargain with the lenders. So that is not fully capitalized. So we feel next financial year, just to give a number, Q3, we raised more than INR1,000 crores, and Q4, we raised more than INR1,500 crores of liability. So I don't think that liability is going to be any challenge. And the customers whom we lend, they are not rate sensitive, so I don't think even borrowing from lenders will not have any impact on our growth.

Moderator: Next question is from the line of Manish Ostwal from Nirmal Bang. Please go ahead.

Manish Ostwal: My question on our loan pricing mechanism. So we generate on a portfolio yield of 24%, and we have a credit losses 0.72% for the last year and this year also even lower than that. So my question is, from a risk-adjusted perspective, since we are pricing almost 2% a month on a loan product. So what would be the sustainable trade cost for the business model, what we operate at Five-Star? And secondly, what is your comfortable leverage on the balance sheet. Currently, it is 2x of the net worth. So what is the comfortable leverage we can assume for the business?

Srikanth Gopalakrishnan: I think the guidance that we have been giving on the credit cost, while it has been swinging a little bit over the last few years, given the first wave of COVID, second wave of COVID, companies building up provisions in anticipation of certain stress in their portfolio. So our guidance to you on the credit cost will be 75 to 100 basis points is what you should probably plan. While 72 basis points was for financial year 2022. And like I said, in FY '20, '21 and '22, we had upfronted some of our provisions, anticipating stress because of COVID, because of the changed regulatory norms and all that, but that is now over. So the 38 basis points is for the quarter and 29 basis points for the year is also because of us upfronting certain provisions in the previous years. But this number will go up as we get into the future. So from a modelling perspective, we'll guide you for a 75 to 100 basis points of credit cost, which is something that we can comfortably absorb in our P&L.

In terms of the second question, from a leverage perspective, see, we are at 2x of leverage today. Historically, over the last 10, 12 years, if you look at, Five-Star has been comfortable operating around the 4 to 4.5x of leverage, which means a 3 to 3.5x of debt equity. And I think that is the level that we will be comfortable and we are targeting to achieve in the next few years. Given the strength of our networth and the internal accruals that we keep doing on a year-on-year basis, it is going to take a little time for us to reach this level, but I think we will be comfortable operating at around the 4 to 4.5x leverage, translating roughly to 3 to 3.5x of debt equity.

Manish Ostwal: Second, sir, in terms of looking at our profitability and the ROE metrics, there is a -- I believe there is a -- still there is a room for our cost of borrowing to reduce further given the profitability and the capital adequacy positioning. So what's your comment on that, sir?

Srikanth Gopalakrishnan: Yes, I got the question. We got the question. See, currently, our book is running at 10.1%. And like I said, we are borrowing at around 9.5% to 9.75%. So there is still some minor benefit that is available. Maybe this 10.1% will probably drop to about 10% or maybe another 10, 15 basis points. So today, if you look at our spreads, we are at about 14%. But what we have also been guiding is that wanting to be a responsible institution, I think as we go forward, we will -- once we have seen the peak and the rates start stabilizing or start easing up, we will also want to pass on some of these benefits to our borrowers.

So our steady state while we are guiding you for the spreads will be about 12% to 13%. So there will be some benefit coming from cost of funds dropping in the future and also some impact coming on account of us dropping the yields, but we will be comfortable operating around the 12 to 13 kind of percent spread. If you look at FY '22, we were at about 13.5%. So maybe around 13% is where the company has operated in the last many years, and that's something that we'll also be comfortable operating at. There is some benefit that may come in from liabilities, like Mr. Pathy said, given our rating upgrades and the fact that we have looked at as a very safe institution by the banks and financial institutions, but I don't see significant benefit coming in the next financial year. So 10.1% may go down by maybe another 20, 25 basis points.

Manish Ostwal: Sure. And last, very quickly, what is the guidance for the branch expansion for the next year?

Lakshmipathy Deenadayalan: So Manish, the quick guidance, what we always keep saying is we'll be adding close to 50 to 60 branches year-on-year. That's a very important lever for us for registering a 30%-plus growth year-on-year. So that's our guidance for the short-term.

Moderator: The next question is from the line of Parag Jariwala from White Oak Capital. Please go ahead.

Parag Jariwala: Yes, continuing the same question. If I look at, let's say, over the next 2, 3 years, where do you see because many of the branches which we opened in the last 1, 1.5 years would have not fully matured in terms of business they do. So over the next 2, 3 years, where do you see our disbursement as well as the AUM kind of go up from here. If you can broadly just outline the 3 years metrics from here on?

Lakshmipathy Deenadayalan: Yes. So let me start with the disbursement, what you've been talking. See, as I said, the growth factor will come from 3 strong positions of Five-Star. Before that, let me also clarify that Five-Star's presence is strongly in Tier 3 to Tier 7 towns where the stock keeper, self-employed, cash salaries, first port of credit is borrowing from the local people. That is where Five-Star goes and disturbs the market, and we captured the market in these tiers. So I think the first level of growth will come from branch expansion, as I said in earlier question, we'll be opening close to 50, 60 branches year-on-year.

Just to take you a data. Last year, we said we opened 73 branches. And out of that, 96% of the branches have achieved breakeven in past 6 to 9 months. So that shows the strong opportunity potential that what we have in the local market to disturb the local markets credit. So as we move forward for the next 2 to 3 years, I said branch opening, addition of people, feet on street and a slight increase in average ticket size. We have moved our average ticket size from INR3 lakh to close to 3.3 lakhs taking inflation into account. So putting all these 3 things together in the next 2 to 3 years, we can very comfortably grow at 30% plus without any disturbance.

And as I said, our collections also have moved up very well in last 2 quarters, especially after the new RBI guidelines came in, which was a little bit of threat for the retail lending segment, but we did very well. Our strategy worked very well. So we dropped down that even from 1.42% -- 1.46% to 1.32% now. So we feel very comfortable both in opportunity, our execution and collections. So we can very strongly give a guidance of 30% plus year-on-year growth in next 2 to 3 years.

Parag Jariwala: Perfect.

Moderator: Next question is from the line of Chandrasekhar Sridhar from Fidelity International. Please go ahead.

Chandrasekhar Sridhar: I had a few questions. First, Srikanth. Srikanth, I noticed the share of fixed rate borrowings actually come down. Maybe you can just help me understand what is the share of -- how do you all think sort of medium, long-term, just the share of fixed rate borrowing in the book? And what's the average rate on your fixed rates borrowing at this point? And then just in that context also, maybe it's worthwhile just sharing the composition of the liability book on how much securitization, how much -- I mean, I think you mentioned banks as a certain number, but just banks and securitization, I think that will be a little useful.

Srikanth Gopalakrishnan: Sure. So Chandra, yes, the fixed rate borrowings are coming down because we are more and more borrowing term loans from banks. But the good part is, we are not linking our -- the rates to the repo, which typically tends to move faster and move much quicker. Our borrowings are linked to the MCLR of the banks either at 6 months or 1-year interval. So we are definitely not going to see very, very frequent interest rate movements that may be happening. So our guidance is - typically most of the securitization transactions tend to be fixed. NCDs are fixed, but we have not been too active in the NCD market. So I think I would probably guide you to something around 25% to 30% of fixed rate borrowings in a steady state scenario with about 70% to 75% coming through the variable rate model.

In terms of the cost of funds on the fixed rate borrowings, Chandra, I think these are largely around 9.25% to 9.50%. So at this point of time or at the time of origination, we actually don't see too much of a difference between a fixed rate borrowing versus a variable rate borrowing. Like I said, fixed rate borrowings are typically the PTC transactions, where the initial -- the rate tends to be lower, but you also have the other parts in terms of the negative carry on the credit enhancements, you have the rating and other expenses, which tends to push up the cost to about 9.50% also. So you will typically see fixed rate borrowings and variable rate borrowings broadly at around the 9.40%, 9.50% levels, give or take 10 basis points this way, that way depending on which lender comes in, what quantums and all that. Typically, we tend to pay some premium for very strong lenders or for significantly higher quantums.

From a structure perspective, Chandra, I think this is part of our presentation as well. So if you look at March 23, 56% of our borrowings have come in in the form of bank term loans, 6% are from other term loans. Typically, the larger NBFCs like Bajaj and Cholas of the world. We have 12% NCD issuances that we have done and 23% where we have borrowed through the PTC, the securitization route and about 2% in the form of ECB. So our guidance typically has also been that other than bank term loans, be it NCDs or securitization, we'll typically want to keep this at around 30% levels -- 25% to 30% levels in a steady state scenario.

The bank term loans, we are even happy to take it up to 55%, 60% because that is one form of borrowing where we feel it is highly sticky. There are no kneejerk reactions depending on how the economy moves or if there is any event risk that comes through. So I think we'll continue to target the NCD market, one of the places where we probably don't have today is a lot of AMCs taking -- subscribing to our NCDs. I think that is one thing that we will target in the coming year. And securitization, people are, you know there are many takers for the company's assets given the strong quality. So we will continue to explore securitization. And obviously, with the preference -- the first preference being for term loans from banks.

Chandrasekhar Sridhar: Sure. Can you just share maybe the duration of the asset and the liability book at this point in time?

Srikanth Gopalakrishnan: So the duration of the asset, Chandra, like we say, adjusted for prepayments. While on origination, it's around 6, 6.5 years. But adjusted for prepayments, typically, we see this number around 4.5 years. On the liabilities, there's no question of prepayments. Today, the good part is we are also getting liabilities for 7 years. We have recently gotten a 7-year sanction from one of the largest public sector banks. So the average duration is roughly about 4 years.

Chandrasekhar Sridhar: Okay. Okay, got it. Can you -- for Mr. Pathy maybe just a couple of questions. Just the AUM is greater than 5-year vintage, branches has now stayed constant for some time. Is this a function of maybe splitting some of these larger branches or that's the sort of given the resources which you add in the branch that that's a maximum sort of AUM you can have per branch? And secondly, obviously, this collection vertical where we are adding people and it was -- a lot of it was front-ended we were adding. Just where are we in the process and how far do we have to go to sort of for the employees in the collection vertical to catch up with the vintages cases?

Lakshmipathy Deenadayalan: Yes. I'll invite Ranga to answer on both the questions.

Rangarajan Krishnan: Chandra, the first question, your observation is right. We had explained this in the past conference call also. We believe that when a branch crosses a particular threshold in terms of assets, it's better from a risk management perspective to split the branch, wherein we can open two or three neighbourhood branches and then split the new branches along with a certain set of accounts, which are more closer to the vicinity of the branch. So whenever a branch, let's say, crosses 1,500, 2,000 accounts, what we tend to do is we'll open 1 or 2 branches nearby. And on day one, these branches will start with 300-400 accounts.

So optically, it looks as if the 5-year-old or the larger branches are not moving in, but that's not the case. To really go through the true growth of those branches, we'll have to combine any child branches which have originated from these parent branches and then put it together to get the real picture. This is something that we routinely do because it helps us manage risk far better, no concentration risk for us. More importantly, it also helps us promote our employees where the branch performs very well, and they have been consistently doing good. We will identify high-performing officers in -- from the same branch and then promote them as branch managers in the vicinity branches. And then they will take off from there. So it's not true that the branches are sort of flattening beyond 5 years. It continues to grow at a healthy pace.

Now, on second, the collection vertical, we had updated earlier that the collection vertical formation is complete in Tamil Nadu and we had started off that in Telangana. Now Telangana is also almost complete. We wanted to wait and watch to see how these 2 states are behaving from a stability perspective post the collections vertical, from a cost perspective, from collection efficiencies perspective, and any disruption that we are seeing in the business. We're happy to report that across various internal benchmarks and metrics, it has yielded extremely good results for us. Two large states are taken care. I think the only other large state which is remaining is Andhra Pradesh and where we will be doing it gradually over the next few quarters.

Chandrasekhar Sridhar: Great. Very useful. Maybe if I can just squeeze in a very last one. Just why has this Stage 3 PCR gone up?

Srikanth Gopalakrishnan: Can you repeat, Chandra?

Chandrasekhar Sridhar: Why has this Stage 3 PCR gone up?

Srikanth Gopalakrishnan: So Chandra, that's purely a function of the ECL model that we are actually seeing. We are also trying to create a little more on the restructured book. So while the LGD on Stage 3 is still fairly muted, we are targeting any deep delinquent accounts, like loans, which are more than 450 days are provided at close to 100%, Stage 3 restructured assets are provided for at 100%. So we are consciously creating a lot more overlays on the Stage 3 assets, especially on deep delinquent accounts and restructured assets, which is why you see -- and the NPAs are a little sticky for us, right? While you don't see incremental NPAs coming through, it takes time for a resolution of these NPAs. So when it keeps going into the 450+ DPD kind of a number, you tend to create more PCR. So the PCR is purely a function of the LGDs, restructuring and the DPD of the assets, the Stage 3 assets.

Lakshmipathy Deenadayalan: Chandra, let me also add, it's very prudent to increase your provision in Stage 3 assets. So that was one point. That has also resulted in the reasons what Srikanth said, that was also resulted in the gross Stage 3 versus net stage 3. If you see gross is 1.36% versus net of 0.69%. It takes cares of 49% of that is being provided for. So we think it's very prudent method to follow this, especially when the restructured books are getting matured and moratorium accounts are getting matured. So we want to have a very conservative approach, and we'll see how the next few quarters behave.

Chandrasekhar Sridhar: Yes. So basically, this is not like a longer-term steady state. It's basically some of the function of the restructured accounts and moratorium accounts more than anything else? These are a function of the account maturity more than anything else. In longer-term, you're still sort of -- you should be running at lower PCRs…

Srikanth Gopalakrishnan: Yes, Chandra, don't take this as a guidance. I think our steady state guidance will be more like about 35% to 40% PCR on Stage 3 as against what we are seeing today, which is a little inflated because of the reasons that we explained.

Moderator: The next question is from the line of Arjun Bagga from Baroda BNP Paribas. Please go ahead.

Arjun Bagga: Congratulations on a good set of numbers. Just one question out here. Just wanted to understand that I think the cash for us has gone up from some INR900 crores in the last quarter to some INR1,500 crores, INR1,600 crores. So if you could just help me understand what is this due to? And going forward, what should be a steady state number that we can expect?

Srikanth Gopalakrishnan: So Arjun, I think this is a conscious call that we took during the quarter for 3 reasons. One is we are expecting a strong quarter in Q1 as well, where you will see a good amount of disbursals, there could be some muting as compared to the Q4, but you will still see a much stronger quarter as compared to any other typical Q1s that we have seen in the past. So for which we need to build adequate liquidity. And all of us know that, typically, the first quarter tends to be a little muted from a bank borrowing perspective. So very clearly, expecting a strong quarter is where we have built this adequate liquidity for us.

Yes, our liquidity policy is fairly straightforward, Arjun. We will endeavour to maintain 3 months operational expenses, 3 months debt repayments and 1 month of projected disbursals, which today roughly works to about INR900 crores to INR1,000 crores. So that will probably be the number that we'll want to be at. The other reason why we also built a little more liquidity in Q4 of this year is also because of certain chunkier repayments that are coming up in the month of April and May. We had done few NCD and covered bond transactions in the past. Those are coming up for maturity. So those will amount to roughly about INR350 crores to INR400 crores. So there is a bit of excess liquidity that we have maintained to ensure repayment of these borrowings.

So it's a combination of repayments coming up. The stronger quarter that we are expecting in the current -- the first quarter. And lastly, banks being more active in Q4 and being muted in Q1. So you will always see Q4 being a little steep, but I think we will endeavour to maintain about INR1,000 crores -- INR1,000 crores to INR1,200crores of liquidity on a steady state basis at least for this year.

Arjun Bagga: Sure, sir. This is helpful.

Moderator: Next question is from the line of Amit Mantri from 2Point2 Capital. Please go ahead.

Amit Mantri: I had just one question on the state-wise growth. So Andhra Pradesh has seen a very strong growth this year, almost 50%. So can you talk a bit about what's happening in Andhra Pradesh that's driving the strong growth in loan book?

Rangarajan Krishnan: Amit, this was a conscious call that we had taken last year. So we saw Andhra Pradesh showing extremely good results. We have built great teams there. So last year, as a conscious strategy, we opened the highest number of branches in Andhra Pradesh. We opened close to 41 branches in a single state, and happy to report that all the branches have performed extremely well and are well set. So that is the effort that you see in disbursements coming from Andhra Pradesh because of this.

Lakshmipathy Deenadayalan: And just to add a little bit of more state colour, see, for Five-Star, we are a predominant south-based where we are in -- present in Tamil Nadu, Andhra, Telangana and Karnataka. Tamil Nadu, as our home state, will always perform well. And Andhra and Telangana are the states where the performance is very good. And one state I wanted to put a note here is Karnataka, which was a little muted during COVID. Pre-COVID it was doing well, whereas in the COVID period, it was little muted, but happy to say that Karnataka has also come aligned with all other 3 states of South.

So going forward, as we say, 50 to 60 branches what we intend to put in minimum. Karnataka will also add up in the line. So you have -- this year, you'll have a good spread of branches across Tamil Nadu, Andhra, Telangana and Karnataka. And definitely, having said that, we have a high scope in non-South also. So today, our non-South, MP, MH, Chhattisgarh, all put together, we have close to 50, 55 branches across non-South. So that will also keep growing.

And we'll also be putting our feet in very important states like Rajasthan and Gujarat, where we will be starting learning about their ground level behavioural aspect, customers, repayments, legal nuances. So we will put our few branches in Rajasthan and Gujarat in this year, and we'll wait and see how that behaves. So that's the broad state input. But last year, we have invested a little -- a lot -- more in Andhra. We felt there is more opportunity, and that has yielded a good growth in Andhra. That's why you see Andhra a little spurt in last year. But this year, we see across all states, the growth will be there.

Moderator: Next question is from the line of Shubhranshu Mishra from Phillip Capital. Please go ahead.

Shubhranshu Mishra: So the first question is on the rejections ratios. What's the kind of rejection ratios that we have in the top three states, which is Tamil Nadu, Karnataka and Andhra. Second is, we have certain number of mature branches. What is the total number of mature branches and what is their profit contribution? The third question is, what is the total number of cases that have got resolved in SARFAESI since our inception and post-COVID?

Rangarajan Krishnan: Yes. So let me -- your first question was not clear. So let me start with the third question, what is the number of SARFAESI cases that we have initiated since inception? SARFAESI is applicable only for loans of INR20 lakhs and above. So our average ticket sales is INR3 lakhs to INR5 lakhs. So we are not covered by SARFAESI for a good chunk of our loans, except for hardly about 2%, 3% of our loans, which will potentially be above INR20 lakhs as well.

But that said, we had started initiating SARFAESI proceedings against these loans, whatever handful of loans that we have above INR20 lakhs. In the last quarter, we have had some good results. We didn't need to go to the auction part, but I think these 4 accounts -- 3 to 4 accounts got settled, right, after we initiated the SARFAESI, notices to the customers themselves. But it's not a big part of our strategy, given that extremely -- hardly less than 1% to 2% of our loans fall in the SARFAESI category.

Lakshmipathy Deenadayalan: Just to add on this third question -- or this question, Mishra, you can repeat the first question again. On the SARFAESI or repossession or sale, I think we have been telling constantly to the market, and all of the conference call that, in last 20 years, we have been in this business, we have not done a physical repossession yet. That doesn't mean that our accounts are not meant for repossession. We do a technical repossession, which we explained in detail in last or before that. When an account becomes NPA or 90-plus, the legal proceeding starts. We have all right to take the property to the auction and we know how the property can be taken to the auction route. So we move the customer and property to the arbitration.

We take the arbitration decree quickly and we file EP petition in the local jurisdiction court. That gives us the right to take the possession and sell the property in the market. By doing this method, we strongly feel the value of the property is going to go down at least 50%, 60% of the market value. Neither the customer, nor the company is going to benefit out of this. What is the strategy that we have been adopting for last many, many years, which has resulted in a very good recovery from NPA, both in principal and the IRR, we keep negotiating with the customer once the legal notice is sent to them and we discuss with them about the inability of the repayment and taking the property to the market by the customer itself. That protects the market value of the property.

Hence when the customer takes the property to the market, it will not happen immediately. It will take 18 to 24 months when we keep negotiating with the customer. So when he takes the property to the market, he gets the full value of the property because market, they don't know the property is brought to the market as a distress sale. It has been brought to the market as a normal sale. So he gets the full value of the property. At that point of time, our debt will be 35%; his equity will be 65%, and very comfortably he'll be paying back our debt with close to the contracted IRR, and he will take away the 65% of the capital and he'll move on to the second life, where he intend to do.

So by this method, it's a win-win for both the customer as well as the company. We get our principal and contracted IRR; customer gets a good chunk of sale, what he gets from the market value and he restarts the second life. I think that is where we have also put in in DRHP close to 4,000 accounts, which got settled by this technical repossession or sale where we were able to get back close to our contracted IRR, close to 22% we were able to recover from this deep delinquent accounts. So that is the strategy, which is working well because these customers are not intentional defaulters. There's only a delay, which has happened for various factors. I think this is where Five-Star's focus will be.

Having said this, we have also put in our legal recovery vertical for last few quarters. Chief Legal Officer has joined. With that very strong now, more and more properties, you'll see going to the EP level, but we have to wait and see how many properties that we'll be selling or we'll be making the customer to sell.

Shubhranshu Mishra: Right. And the first two questions on rejection ratio and mature branches' profit contribution?

Lakshmipathy Deenadayalan: Rejection ratio and mature branches profit.

Rangarajan Krishnan: Yes. Shubhranshu, the general rejection ratio that we see, we start measuring rejection ratio at 2 levels. One is what is the rejection ratio that happens before the login and second is what happens after the login. So prior to the login, we go to great lengths to actually teach our people to ensure that the right files are logged in so that nobody is wasting time on a wrong file. So even prior to the login, we ask the people to go and our people to go and visit the place of business, place of residence and take a calculated call whether this file is likely to get approved. This way, most of the filtration gets done pre-login stage itself. Hence, you will see that at the pre-login stage, our rejection ratios are anywhere between 30% to 40%.

But once the file is logged in, the -- maybe the quantum of loans and the customers requesting could get reduced, but we will at least see 80% of the files getting approved at this stage from a login to sanction perspective. So the rejection ratios are about 20% at this stage post the login. This is similar across all the states. There is no big differences between different states here. Maybe some new branches, it could be a little higher, but wherever we see the rejection ratios are higher than the 20%

spurt, we will get into the details, maybe giving more training, ask him to go to another branch, and then shadow the existing team for a few weeks. So all that gets done, but on an average, it's about 20%.

Shubhranshu Mishra: And the number of branches, which are mature and their profit contribution?

Rangarajan Krishnan: So when you say mature, the way we measure is that any branch on an average breaks even between 6 to 9 months from inception. So if a branch reaches a assets under management of about INR 2.5 crores, they break even at a branch level. At anywhere between 6 to 9 months, we have consistently seen that the branch has reached this point of time, and beyond that, they become contributing branches. So this is one point that Mr. Pathy also was explaining that out of all the branches that we opened last year, 96% of the branches have crossed INR 2 crores to INR2.5 crores of portfolio within the same 6-month mark that we had.

To be precise, except for 1 branch, which took maybe 9 to 10 months to reach this level, every other branch has crossed this level, which means every branch, these are very, very asset-light branches and they start contributing from day 1. So we reach maturity level at a breakeven perspective fairly fast at a branch level. From that perspective, every branch is a contributing branch. Beyond that, it really depends on whether it's a normal branch, super-branch, it's a parent branch, child branch. There are multiple variables within that. So it's not a straight answer for your question. But we don't have loss-making branches or pure collection branches at Five-Star.

Shubhranshu Mishra: Understood. And if I can just squeeze in one last question, sir, how do we avoid fraud or any inaccuracy in the valuation of the property? How many people we deploy in audit and for the -- for this purpose or any external valuation we do of the property?

Rangarajan Krishnan: So the entire checking, underwriting and the valuation of the property is done in-house. We don't employ any third-party agencies because we believe that people who are in your full-time role are more controllable and collusion will be far lesser. So the checking happens at 2 different departments. One is the business team, which logs in the file. Even at the business team, the officer who logs in the file is the first person who checks the file. That file has to get finally recommended by the chief of the branch, which is the branch manager, who will also go personally visit this file, do a valuation exercise, do a character assessment, do a cash flow assessment, and finally, recommend that file from his perspective. None of the people in the business side has any approval from it. So from the business team, there is a minimum of 2 people who checks every file that gets logged in.

But like I said, they don't have an approval power. The file then moves to the credit team. Now, our credit team, we again have 2 people. One person is called the field credit. So every branch has a field credit. They don't report to the business at all. They will do an independent assessment of this file. They don't get access to what assessment has been done by the business team. They will do an independent assessment of this file across all the 3 parameters. And they will submit their report to the senior person in the credit, which is called the file credit or the approval credit. They will finally check all the parameters and then give an approval. This approval credit is more centralized or based out of regional offices of Five-Star, but it is state wise, at various regional offices of Five-Star.

So between these 4 pairs of eyes, it's very difficult for a wrong document or a fraudulent document to get inside, especially when credit team has no incentive on the quantum of business gets done or the amount of approvals, which gets done. Credit team's incentives are purely based on productivity metrics. They get equal incentives for a rejected file or for an approved file. So we have not seen any great fraud documents which are coming here. Two additional checks, which also gets done post the sanction by the credit team is one by the operations team, where the physical file finally comes to the head office in Chennai. Every file is checked here clearly before the disbursement happens.

And second, because it's a mortgage-backed loan that we are giving, the mortgage has to be registered with the government agency. So for whatever reason if the document is a fraud, the government is unlikely to accept the mortgage done on a fraudulent document. So that acts as an indirect checkpoint for us also. So only after all these layers are created and passed through, a final loan sanction happens.

Lakshmipathy Deenadayalan: So just to add one -- two point on what Ranga said in detail about how frauds are less, first is very simple. Fraud doesn't happen for a small ticket loan -- small ticket size loan. Our average ticket size is INR3 lakhs to INR3.5 lakhs. So generally, frauds don't happen at a smaller ticket size loans. Having said that, the valuation part what you mentioned, we have 2 teams, as Ranga shared, business and credit. Both check the valuation. They check last 3 transaction happened in the locality, what is the last 3 transaction happened, both purchased and sold. They take the lowest out of that. That we call as the market value.

From there, 20% knock-down has been put in place, that we call a distressed value. So market value is INR100 means the distressed value will be taken as INR80. From there, the LTV, loan to value is only 50%. So it is INR40 that we lend on that property. So that too done by 2 teams, one is business and credit. We take the lowest of both. And I think in last 20 years, we would have seen a handful of frauds, which is happening, in a year 1 or 2, for -- close addition of 1 lakh loans to Five-Star, we have 1 or 2 in a year. So I think this is how the fraudulent activity has been controlled in the small files.

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

Raghav Garg: I just wanted to understand a bit more on your branches strategy and that too state-wise. So when I look at your number of branches per district historically, that's been about 2 per district. Even FY '22, we were at that level. But when I look at state specific data, it seems that your branch presence in each district in Andhra Pradesh is more dense, in the sense that your presence in Andhra Pradesh districts is more dense, having about 4 branches per district. So could you explain how do you define state-specific strategy as far as the branch density is concerned? And then I have another follow-up question.

Rangarajan Krishnan: So Raghav, thanks for the question. We had clarified this in the past. We don't have any rule internally that every district has to be penetrated and each district has to have only 1 branch or 2 branches. The potential of a state or the potential of a region is seen by the number of rising towns, municipalities, which are there where today we go up to Tier 6 and Tier 7 towns. So any town, which is defined as having population of greater than 20,000, 25,000, with good retail activity where other NBFCs are present, that's a possibility for us. And secondly, like I said, if a branch is very successful, we can easily open 3 to 4 branches right in the vicinity.

So the district penetration or density is something that does not get into our mind space, while actually deciding how many branches to put. It's more about population, it's more about repayment data, it's more about other -- presence of other NBFCs and banks in a particular locality. That is what is more important for us to decide on a particular branch location. So Andhra Pradesh, from that perspective, we still believe there are a lot of other towns potential, where we can potentially get into. There is no perspective of reaching anywhere close to saturation at this point of time. We will continue to adopt the same methodology as far as the branch expansion is concerned.

Raghav Garg: Sure. Could you help us with the number of districts for at least the southern states, if you have that data available readily with you, the number of districts that you're present in?

Rangarajan Krishnan: Yes. So Raghav, we just explained that that doesn't get into our decision-making stream at all. So it's more about towns, population and tiers of towns.

Lakshmipathy Deenadayalan: So having said that, Raghav, I think we'd be present in almost all districts in Andhra, almost all districts in Tamil Nadu, almost all districts in Telangana, just to give a perspective. And as Ranga very clearly said, population is the metric for us. If a town has a population of more than 25,000, Five-Star's presence will be there to disturb the local credit prevailing there. So that's our model. That is yielding us very well, where the other competitor's penetration is not so. They stay in Tier 1 and Tier 2 whereas our model is Tier 3 to Tier 6 towns where we penetrate. So capturing the towns is more important for us rather than saying from a district perspective. So having said that, we are present in all districts in 3 major states in south.

Moderator: The next question is from the line of Piran Engineer from CLSA India. Please go ahead.

Piran Engineer: Yes. Congrats on the quarter. Just a couple of questions. Firstly, there was this RBI discussion paper on penal charges. Let's say that comes into effect, what could be the impact for you all on yield or on fee income?

Srikanth Gopalakrishnan: So Piran, we are not expecting any changes. In fact, if you look at the guidelines that have been issued, which is in the draft stage obviously, we are actually completely compliant to all of that. We don't charge penal interest on the principal outstanding. We charge penal interest only on the overdue instalments for the number of days that it remains overdue. And this is duly disclosed in the fair practice code. So we don't really see any impact. I think the only impact which probably could come through, I think which is also at some discussion state in various forums is the fact that changing the nomenclature from penal interest to penal charges could make this fee subject to GST.

Now, that is going to add another 18% on this amount in the hands of the borrowers. So obviously, any company who's charging this is now going to charge the GST also and collect it from the borrower, which is actually more detrimental to the borrower rather than being in his or her interest. But I believe this is some under discussion. If that comes through, we'll also have to charge GST on them and pay it down, but other than that, we are completely compliant and don't see any kind of an impact coming up for us.

Lakshmipathy Deenadayalan: So in short, there is no impact, zero impact for Five-Star, if it comes. And the good practice what RBI says in the circular, Five-Star has been practicing for the last 20 years. So that's the exact -- the outcome what we expect. So there is no impact at all. As Srikanth said, there may be some impact in the hands of the customer, if RBI is not changing the nomenclature from P&L charges to P&L interest again. That will be 18% impact to the P&L charges in the hands of the customer. That we feel, as a lender to the last resort, we are increasing a little bit of burden to the customers. So that's what our representative associations has made their request to RBI. We'll wait and see.

Piran Engineer: Got it. And secondly also, our employee expenses have tapered off a bit despite adding more employees. So any one-off here?

Srikanth Gopalakrishnan: So Piran, you're comparing current quarter to previous quarter or quarter-on-quarter?

Piran Engineer: Yes, Q-o-Q. Yes.

Srikanth Gopalakrishnan: So like last time we did mention, Piran, we had given a one-time -- in the December quarter, we had given one-time payment to the employees for the successful completion of IPO, so which is 1 month's salary. So it's typically 4 months' salary against 3 months' salary that you are looking at, which is where it has tapered off a little bit.

Piran Engineer: Okay. That makes sense. I forgot that. Just lastly, in terms of your 3 lakh customers, if I have to just think about how many of them are repeat. And do you also track if a customer finishes her loan with you, does he continue on another loan with you or does he move to another lender in the system, maybe a small finance bank or a bank?

Srikanth Gopalakrishnan: So Piran, I think this is a question that you had asked us, I think, 2 quarters back as well. See, what we typically see is at a point of time, and I'm talking as of March, we have about 20,000 to 25,000 customers who are actually running multiple loans with the company. So these are people who will have most likely 2 loans. So that is the customers who are topup -- what we call as topup customers, people who have a loan, they have a fresh requirement, they come, and then we give a fresh loan to them and both the loans run simultaneously. What we've also seen is -- in the past is that there are another 20,000 odd customers who had actually closed their loans in the past and come and have taken a fresh loan with the -- fresh loans with the company.

So they are what you call as repeat customers. They might have matured their -- their earlier loan could have matured or they could have pre-closed their earlier loan, and come and taken a fresh loan from Five-Star. So what you're talking is about 30,000 to 40,000 customers who could be various forms of top-ups or repeats. Anecdotally, what we believe, Piran, and this is something where we don't have empirical data to prove, but then what we have seen in our experience is that, if we onboard 100 customers, and these are largely customers from the unorganized institutions, you do see that about 10% of the customers graduate to the formal institutions.

Like you said, the larger NBFCs, small finance banks or banks, because they are able to pay perfectly well for the 84 months. Their records are there in the credit bureau and their requirement for loan is much higher, which is met by a larger NBFC or a small finance bank. We also see about 10% of our customers going back to the unorganized lending because they are not able to stand the rigor of the collections follow-up that we do and all that. 80% of the customers typically tend to stick with us.

So either they will close -- they will get their loan matured, come back for another loan, which is, I think, over the next few years, we will see that happening a lot more because it's a 5 to 7-year loan and our growth has come in largely in the last about 5 to 7 years. Plus we also see, like I said, people who will pre-close their loans ahead of their tenure and then come and take loans from us. So the 80% typically continues to stay with Five-Star in various forms, but like I said, this is more from the company's experience and we don't have empirical evidence to sort of show this data.

Moderator: Next question is from the line of Abhishek, an Individual Investor.

Abhishek: Yes. Congratulations on a wonderful quarter. I just wanted to know like these fintechs are now also lending to the unlent people, what Lakshmipathy was saying earlier. So how do you see the competition from the -- these Paytm kind of companies? Because they also are having a data about the customers or these online people, marginal people. Number one. Number two question is, on your presentation, Page 40, there is a gross Stage 3 assets with a 2-year lag, and the percentage is around 2.11%. So basically, obviously that is after RBI reclassification, but I want to say that if that is 2.11% with reference to the loans that you had 2 years ago, it's a much higher percentage. Do you see -- is it due to any accounting norm or do you see that percentage remaining at -- 1-year lag is around 1.85%, that is page 40 from your presentation. So just these two questions, fintechs and this gross Stage 3 assets?

Lakshmipathy Deenadayalan: I'll ask Srikanth to take the second question and will come back on the first question.

Srikanth Gopalakrishnan: Yes. So see, I think the lag NPA, the way what we have presented is that a company which is growing significantly fast, the NPAs could tend to get camouflaged because of the growth, which is why every NBFC looks at a lag NPA, and what it means by lag -- what we mean by lag NPA is NPA as of 31st March 2023. A 2-year lag means you're comparing it against the portfolio as of 31st March 2021. So effectively whatever loans that we have onboarded in the last 2 years, you don't really give any benefit at all. Those loans could have turned NPA and maybe they're in the numerator, but you don't give the benefit of the denominator, which is why the 1.04%, what 90-plus is as of 31st March, looks at 2.11% from a lag perspective.

So if you really look at it, this is a very, very healthy number. 2-year lag means we have probably disbursed INR1,750 crores in FY '22 and about INR3,300 crores in FY '23. This entire INR5,000 crores of disbursals is not even forming part of the denominator, which was about INR4,400 crores as of FY 2021, whereas the numerator is INR93 crores, which is NPAs as of 31st March. So it is not a high number at all. It is actually a very, very low number.

Abhishek: Any idea about the industry number for this lag?

Lakshmipathy Deenadayalan: So I think we can't say any industry number. I think you can go and calculate. As Srikanth said, it is a pure mathematic calculation. Denominator takes 2 years back AUM and numerator takes the current 90-plus.

Srikanth Gopalakrishnan: Abhishek, there are companies whose current NPAs, what typically is called as coincidental NPAs, NPA as of 31st March as a percentage of 31st March portfolio, most of the companies are more than 2%. What we are saying is our lag NPA is 2% lagged by 2 years. So that is the comparison.

Lakshmipathy Deenadayalan: So I think that will be one of the best in the industry for the customers whom we cater to. That's the second question. On the first question, let me also add -- invite Ranga for further adding. To give a context on that, see, people compare Five-Star with fintechs. I think 2 things that we vary large with them. One is the place of presence. Their place of presence in Tier 1 and Tier 2, our place of presence is some Tier 3 to Tier 7, which we said. So they are not present at all. That is one big difference.

Second difference is that their product is completely different. Their product is lending to a working capital need of a business customer. Our product is lending to the business needs of the business customer. Both are different. Once the business is set up, then the working capital requirement comes in. We go at the first instant to help the customer to set up the business. So the product itself is different. And to add more to the product, their product is -- their ticket size will be around INR50,000 to INR100,000, whereas our ticket size is close to INR3 lakhs to INR3.5 lakhs.

And their tenure will be very short, 6 months to 8 months because it's a working capital. Our tenure will be close to 7 years. And they operate in fully unsecured segment, being a working capital lending. Our segment is fully secured. So I think fintechs are no threat for Five-Star both in presence, where we operate and they operate, and the product in what they give to a business customer versus what we give to the business customer. So broadly they are in a different market and we are in a different market. Finally, to end, even if you compare with fintechs, I think the collections what a traditional NBFC like Five-Star does and profitability what we bring on table and asset quality what we mentioned earlier, I don't think they are nowhere even nearer to the traditional NBFCs.

Abhishek: Great. I'll just request you people to make Five-Star a little more presentable to the investor community because if you are doing such a great work, but it is not recognized, ultimately at the end of the day, no -- because to be very frank, I have come across Five-Star, I stayed here for like -- invested for more than a year, but you just need to bring your presence to the investor community, whatever campaign you feel better, like you should get noted, really. That's appreciable.

Lakshmipathy Deenadayalan: Yes. Thank you, Abhishek. Point is noted. We are already doing it. We'll further do it in a more thoughtful way.

Moderator: Next question is from the line of Nischint Chawathe from Kotak Institutional Equities. Please go ahead.

Nischint Chawathe: Thanks. My questions have been answered.

Moderator: Next question is from the line of Vignesh Iyer from Sequent Investments. Please go ahead.

Vignesh Iyer: Congratulations on good set of numbers. Just two questions from my side. The first question is just the rapid expansion, I mean, big expansion that you have done in Andhra Pradesh. Is it a function of the fact that the state government is continuously expanding, I mean, bringing in bigger projects and a certain part of smaller retailers are also getting active and they're going for some kind of loan for doing their businesses or maybe even for any other related purpose? And my second question is, we have got lot of headroom when it comes to taking debt from the market, as you said, up to 4, 4.5 times roughly, you are comfortable with. So what would be the steady-state ROA and ROE that we target maybe 2 year down the line? These are the two questions.

Lakshmipathy Deenadayalan: Yes, Vignesh. We'll answer one by one. First, on the Andhra front, let me clarify to everyone again. The decision what we took to invest more in Andhra purely based on our performance in Andhra;

nothing to do with any state government's intervention into the shopkeepers or anything. So I think all the 4 states from an economy perspective are growing really very well. And Karnataka, if you recollect, in few days back, there was an article in a paper, where the economic activity in Karnataka is extremely high. But as I said, we have not opened a single branch in Karnataka. So it is not the state government or state in total how it performs in economic activity, the Five-Star branch investment will be planned. It's not like that.

It's our own experience in that state, what kind of team that we have set up, what kind of customers that we have lent, and how is the repaying capacity or repayment happening in that state. That decides the number of investments both in branches as well as people we budget year-on-year. I think last year it was thumbs up for Andhra. So we have invested a lot. I've answered that question. This year, the branch expansion and the people expansion will be evenly across all 4 states of south. So that's point number one.

I think I hope that you have -- I have answered the first question. On the second question, we have guided a growth of 30% plus very comfortably in next 2 to 3 years. The game plan is growth. So we will increase our leverage, as Srikanth was already -- gave an indication on the earlier question. With that leverage kicking in in next 2 to 3 years, our return on asset in steady state, if the steady state may kick in 3 years or 5 years down the line, we'll -- steady state on ROA will be close to 6% to 6.5%. Due to the leverage increase in next 3 to 5 years, our ROE will be in 20% plus. That's what we anticipate.

Moderator: The next question is from the line of Nilesh Jethani from BOI AXA Mutual Fund. Please go ahead.

Nilesh Jethani: My first question is from a longer-term outlook, say, from a 3 to 5-year perspective when we talk about 30% growth. So wanted to understand that this would be largely led by a branch-led or the fleet addition on ground or average ticket size because we typically have in the range of 3 to 5 lakh category. Are we planning to expand this range also going forward? So any colour on that from a 3 to 5-year perspective.

Rangarajan Krishnan: Hi, Nilesh. We had sort of covered it in our earnings presentation that we have uploaded. So there are 3 levers to growth for us primarily. The first lever is, of course, the increase in branch presence. So we had already guided for at least adding 50 to 60 branches every year. Last year, we did 73. So we are fairly confident of at least putting up 50 to 60 branches year-on-year. These predominantly will come in south. So we expect at least 80% of the new branch additions to come in from south with 20% contribution from non-south regions. This is the first lever.

The second lever of course is we have constantly strived to increase the number of officers per branch because when a branch is successful and an area is familiar to us, instead of putting up a branch, we always believe that it is better to add more number of people to the existing branches because we are already successful, we are familiar with the area, we have existing customers, business can be done easily in that existing branch. So we have constantly increased the number of officers. Today it averages about a little lower than 8. This will continue to go on. So you will, over the period of time, see this 8 increasing to 9 and 9 increasing to 10. We will not do it in an urgent manner because we don't want to breach the productivity metrics here. But we will ensure that over a period of time, the number of officers in every branch also increases the sales reps from both risk perspective and increasing the potential business that we can do from an existing branch. This is the second lever of growth.

The third lever, of course, is the ticket size. Ticket size, today we are averaging about INR3.2 lakhs in Q4, but pre-COVID, we were already at about INR3.3 lakhs, INR3.5 lakhs. So during COVID, during times of uncertainty, we consciously tightened the credit metrics and we went down all the way to about INR2.5 lakhs of average ticket size. But as the economy is opening up, we have slowly come back to INR3.2 lakhs. The first break for us will be where we are coming back to pre-COVID levels of INR3.3 lakhs to INR3.5 lakhs, which will happen in the next few quarters.

But beyond that, I think ticket size increases will be largely inflationary in nature. We don't intend to move away from this customer bucket because we are very familiar with this customer bucket. We understand them deeply and we have a lot of experience in working with them. So in the same customer bucket, but with a little bit addition of ticket size due to inflationary trends. You will also see some growth for us will be coming in from there. A combination of these 3 is what is making us confident of delivering a 30% plus kind of a growth over the short to medium term.

Nilesh Jethani: Got it. Just to follow up on this, one, let's say hypothetically, if you don't want to add branches going forward, from the same branches, what kind of growth we can expect considering the current AUM per branch? And second follow-up was, in the previous participant response, you had mentioned that repeat customers were in the range of 30,000, 40,000 amongst the 3 lakh customers. The repeat seems to be slightly lower. So what are the -- questions from my side.

Rangarajan Krishnan: See, on the first question, I think if we stop adding branches, hypothetically, I think we'll still be able to deliver maybe about a 20% growth rate, which is the combination of growth lever 1 and growth lever -- growth lever 2 and growth lever 3. Nothing stops us from adding more number of people in the existing branches themselves. Of course, productivity also will see an improvement over a period of time, and the ticket size increases will come. So about 20% growth rate is something that we can see with no addition to the branches at this point of time, in the short to medium term.

And secondly, on the repeat loans, I think the point that you'll have to keep in mind is that our average tenure, like Srikanth had explained earlier, behaviourally it's about 4.5 years. So repeats will come after 4.5 years. Now, we'll have to just retrace our own growth, how big were we 4.5, 5 years back. In 2018, our book size was hardly about INR1,000 crores. So I think you should keep this in mind, while you are looking at a repeat scenario for Five-Star. That is why I think we were explaining it more from a company's experience perspective and how we see customers staying with us moving over a longer period of time.

Nilesh Jethani: Got it. And one last question on the cost side. Any levers to bring down the cost? Because cost to average assets are in the range of 8% for us. So any levers there?

Srikanth Gopalakrishnan: So we do have some benefits -- like if you look at our cost to income, I think we are probably one of the best in the industry in terms of cost to income, given certain manual intensive nature of the activities that we do. Having said that, yes, we are investing in technology. We are doing a lot more projects on the technology side, and we have also significantly invested in the senior management. So both of these are not going to linearly grow with the portfolio. So we will see some benefit coming on the cost of funds, but in terms of opex to assets, I think it will probably drop by another 50 to 75 basis points, but not possible to expect any significant drops to come in the future years.

Moderator: Next question is from the line of Saptarshee Chatterjee from Centrum PMS. Please go ahead.

Saptarshee Chatterjee: My question is on the like operating leverage of the business, and on the growth sustainability. In the sense that, if I see your last 8 years that your AUM have grown more than 50x, but your business officers have grown higher than that. And in the sense that opex has also grown at a higher pace than the AUM. So my question is, today we are at 4,000 number of business officers. Next stage of growth, let's say next 8, 10 years, if we grow 10x at an AUM of current size, will it not be very difficult to have at least on 10x or more than 10x number of business officers hiring and training them? So do you see human capital-intensive businesses like this, like of ours, like acquiring talent can be a challenge for our growth sustainability? And second question is regarding if the acquisition of like business officers grows at a similar pace of AUM, then is there a case of operating leverage?

Lakshmipathy Deenadayalan: See, I'll take up the first question. See, I think from a risk of training perspective, I think I have also addressed in a few calls earlier, so we don't see any underwriting getting diluted both in business and credit vertical, right? That's the foremost concern that the -- outcome of your question as we grow 30% plus in next 3 to 5 years. The very simple answer to that is, see, we want to open 50 to 60 branches year-on-year. So we need 50 to 60 BMs with a very good knowledge on our business model, underwriting, and collections. So today we have close to 4,000 officers, as you said rightly. Picking 40, 50 people from them who is really bright in productivity, who is very good in collections, who maintains the best asset quality, we have the data of 4,000 officers day in, day out on their productivity, collections, and NPA.

So picking the top 50 from the officer and giving him the branch manager's position, it's not going to be a challenge for Five-Star. If a guy is able to do a good productivity, that means he understood who is our customer. If a guy is doing a good collection, that means his assessment on character, cash flow, on collateral, which is a triple C assessment, what we do, has been done well. That is why the outcome is the collections is good. So picking 50 or 60 officers from 4,000 -- a group of 4,000 people and giving them a career growth of branch manager doesn't feel any threat even -- not even today, even going forward. That's on the business side.

From officers side, we don't see much of the knowledge to be gained because they are the connecting between the customers and the branch manager. Branch manager -- for us, the branch manager is the starting point of the knowledge centre, where the underwriting, collections control, attrition, everything has been managed by the branch in charge. So that is where our focus is going to be there. Having said that, officers, we train them to the way that they can be good connected with the local people and distribute our product like customers, how they understand our product better, what is the pricing, that difference between the local money lender and Five-Star, how is the EMI diminishing balance goes well. These are the standard things that we expect our officers to talk with the customers to bring the file to the login.

Then it comes to the hands of the BM. So for us, the BM is the first knowledge centre at a branch. So we don't see, even at 10x growth, our underwriting will get diluted. Even from the credit aspect, that's a separate team which looks into the same triple C approach, both assessing the character, cash flow, and collateral, today we have close to 180 approval credits, not the field credits at the branch. I'm talking about the approval credits who approve the file. Tomorrow, suppose we want to add 20, 25 more to the approval credit, we don't get from the outside.

We know the 350 or 370 people, field credits what we have in the system, we know the best person in the assessment order because we have the data of both each and every field credit. So we take that 20, 25 people from field credit and give them a career improvement to the approval levels. So I don't think as long as our pools both in business and credit is bigger, picking 50 people from that who is the best among the pool and giving them the career growth and taking care of the business and credit vertical, there will not be any dilution in the underwriting even at the 30% growth that what we intend. That's on the question number one.

On the question number two, I'll invite Srikanth to answer on it.

Srikanth Gopalakrishnan: So Saptarshee, like we said, on the operating leverage, see, today at the field level, we have one of the best productivities that you could ever see in this kind of segment. Our officers log in 4 to 5 files, out of which about 4 files get sanctioned and disbursed, so which is one of the best productivities because they are also going to be handling collections for a period of time. Where we think operating leverage will come in, like I said, is in terms of the senior management bandwidth, which is not built for INR7,000 crores company. This is built for a much larger size of Five-Star.

The second will be in terms of technology where we are making significant investments. So we could look at probably down the line looking at straight through processing for certain percentage of files, where today every file is touched by multiple people, at least 4 to 5 people across the business, credit, and approval verticals. We could -- we will be definitely exploring the fact that if we are extremely comfortable with a particular file, does it need to go through this entire chain of business, credit and all this? So this will help us bring in operating leverage. This will also help us cut down the turnaround times.

So some of these things are work in progress and we will probably get to see the results in the next few quarters, but like I guided don't expect significant operating leverage to bring down our cost to assets. Even in a steady state, I think we are expecting our cost to assets to be at around 6% levels, and that is something we are comfortable with. Our P&L has the ability to absorb that and still give a return on assets guidance that Mr. Pathy gave sometime back.

Saptarshee Chatterjee: Great. Just one last question is, as your cost of fund reduces from 10% plus to your current marginal cost of borrowing, so I just want to know your thought process. Will you reduce your yield or will you want to increase your profitability? So if you want to increase your yield and therefore increase that target addressable market or you want to increase your ROE in short to medium term?

Lakshmipathy Deenadayalan: Yes. Thank you for this question. I think this was also addressed in earlier calls. See, 2 years back, our borrowing cost was around 12% on book. That has now brought it down to 10%, roughly around 10%. So we have got a benefit of 200 bps, but we have not passed on this benefit to our customers because we wanted to see where the tip of the curve really stands. As Srikanth said, we are thinking in next 1 or 2 quarters, this will get saturated and we will get a clear indication from the market that there will not be any more increase from regulator or bankers. Once we get that, definitely we'll be bringing down our yields from 24% to close to 23 or even better 22.5%; not to go and capture the bigger market. This is just to be a very responsible lender because the market is huge are -- and people operating in this market, along with Five-Star, are far and few.

Even comparing with them, their quality and profitability is no match with Five-Star. So I don't think there is any pressure from the market to reduce to bring down the pricing. We will be doing it in next few quarters to come, to be a reasonable lender. So that's the point number one. But as a guidance, what Srikanth already said, we will be guiding the market on NIMs close to 14%, 15% and spreads around 13%, 14%. That's the guidance in the long run. So there will be a reduction in yield because we have not transferred our benefit that what we got from our lenders to our borrowers. And of course, the profitability is on a very high side. So we don't have any intent to increase the profitability further. I think that's our clear strategy going forward.

Moderator: Thank you very much. I now hand the conference over to the management for closing comments.

Srikanth Gopalakrishnan: So thank you all for attending this earnings call of the company. Like we said, it has been an extremely strong quarter for us, and we do have the necessary infrastructure built for us. With the clouds of COVID and all the uncertainties receding, we are very confident and hopeful that we will be able to -- we are in a position of strength to take advantage of the market opportunity available. Till we connect with you in the next earnings call, once again, thank you from the management team for taking the time out to look at our results and ask us the questions. Like one individual investor said, our intent is to make you understand our business model.

We'll be happy to address any follow-on questions that you have. The presentation contains the email ID of the Investor Relations team. Feel free to reach out to us and we'll be happy to engage with you. Thank you once again.

Lakshmipathy Deenadayalan: Thank you.

Moderator: Thank you very much. On behalf of Nuvama Institutional Equities, that concludes this conference. Thank you for joining us. You may now disconnect your lines. Thank you.