

**Company Overview**

Northern Arc Capital Ltd. is a diversified financial services platform set up primarily to cater to the diverse retail credit requirements of the under-served households and businesses in India. Over the last 15 years, the company's approach has been to create a differentiated and comprehensive play on the retail credit ecosystem in India spread across sectors. According to the CRISIL Report, the company is among India's diversified NBFCs in terms of AUM as of March 31, 2024, with a business model diversified across offerings, sectors, products, geographies and borrower categories. Further, the company has one of the lowest industry-wide credit costs amongst diversified NBFCs in India as of March 31, 2024. The company has also developed domain expertise in enabling credit across focused sectors in India: MSMEs financing, microfinance (MFI), consumer finance, vehicle finance, affordable housing finance and agricultural finance. The retail credit market in India was Rs. 75.2 trillion as of FY24 and has rapidly grown at a CAGR of 16.0% during FY20 and FY24. The company caters to this retail credit market through a multi-channel approach that includes (i) Lending, Intermediate Retail Lending and Direct to Customer Lending either in collaboration with Retail Lending Partners or through a branch network to offer rural finance and MSME lending, with AUM of Rs. 117,100.19 million across 671 districts, 28 states and seven union territories in India, as of March 31, 2024; (ii) enabling credit for Originator Partners through various financing products Placements, with aggregate Placements volume of Rs. 1,019,039 mn, as of March 31, 2024; and (iii) Fund Management, with aggregate fund deployed of Rs. 120,786 mn across ten alternate investment funds (AIFs) and three portfolio management service (PMS) funds, as of March 31, 2024. The company has built an efficient and scalable business model supported by its proprietary end-to-end integrated technology product suite customized to multiple sectors.

Objects of the issue

The net proceeds from the fresh issue will be used towards the following purposes:

- ⇒ Gross proceeds of the fresh Issue proposes to utilize the Net Proceeds to meet future capital requirements towards onward lending;
- ⇒ General corporate purposes.

Investment Rationale**Wide addressable and underpenetrated market provides ample growth opportunities**

The market for non-banking financial companies (NBFCs) in India is poised for significant growth, driven by affordable data access, digital transformation, and an underpenetrated customer base. NBFCs have generally been able to address this opportunity due to their strong origination skills, extensive reach, better customer service, faster processing, streamlined documentation requirements, digitization of customer onboarding process, customized product offerings, local knowledge, and differentiated credit appraisal methodology. The rapid evolution of Fintechs over the last few years has added another dimension to the market served by NBFCs and has fueled rapid growth across the landscape. Moreover, the Indian retail credit market has grown steadily over the last few years and is expected to grow at a CAGR of 17-18% between FY24 and FY26 to reach Rs. 100.9 trillion by FY26. (Source: CRISIL). The company believes that this presents an opportunity to capitalize on the significant potential for growth in the retail credit market, particularly in the rural and semi-urban areas. By leveraging the company's diversified business model and proprietary technology product suite customized to multiple sectors, it has developed strong sectoral expertise over the last 15 years in enabling credit across focused sectors. We, thus, believe that the company has further solidified its role in facilitating credit across these sectors, positioning itself as a key player in India's rapidly growing retail credit market.

Large ecosystem of partners, data, and technology platforms create strong network effects

The company's technology products and data capabilities are the backbone of the ecosystem, which ensures seamless interaction between Originator Partners, Retail Lending Partners, and Investor Partners, facilitated through the technology platform Nimbus, which enables end-to-end processing of debt transactions. To deepen relationships with Originator Partners, the company has developed a proprietary technology product, Nu Score, a tailored machine learning-based scoring module designed to assist Originator Partners in the loan underwriting process and help them make effective

Issue Details

Offer Period	16 th Sept, 2024 - 19 th Sept, 2024
Price Band	Rs. 249 to Rs. 263
Bid Lot	57
Listing	BSE & NSE
Issue Size (no. of shares in mn)	29.5
Issue Size (Rs. in bn)	7.7
Face Value (Rs.)	10

Issue Structure

QIB	50%
NIB	15%
Retail	35%

BRLM	Axis Capital Ltd; ICICI Securities Ltd; Citigroup Global Markets India Private Ltd.
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Registrar	KFin Technologies Ltd
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Particulars	Pre Issue %	Post Issue %
Promoter & Promoter Group	100.0%	81.7%
Public	0.0%	18.3%
Total	100.00	100.00

(Assuming issue subscribed at higher band)

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credit decisions. Further, to enable technology-backed seamless co-lending across a network of Retail Lending Partners and Investor Partners, the company has developed nPOS. This fully integrated API-based technology solution seamlessly integrates with the systems of Originator Partners (including Retail Lending Partners) and Investor Partners, easing the co-lending process. In addition, AltiFi, an alternative retail debt investment platform, enables them to capture a broader base of retail investors, who may subsequently graduate to invest in funds. These multi-channel offerings, supported by proprietary technology and data capabilities, enable funding to the end customer and aid Originator Partners, Retail Lending Partners and Investor Partners, and AltiFi investors in expanding their outreach and accessing new debt capital pools and investment opportunities. This synergy and seamless integration create a 'flywheel effect', which gets accentuated with more transactions and incremental data flow. This technology-driven ecosystem strengthens the company's competitive positioning, providing a sustainable advantage in the financial ecosystem.

Valuation

Northern Arc Capital Ltd. has a diversified financial services platform set up primarily to cater to the diverse retail credit requirements of India's under-served households and businesses. The company has expertise in lending across various focus sectors in India, especially in micro, small, and medium enterprise (MSME) finance, microfinance (MFI), consumer finance, vehicle finance, affordable housing finance, and agriculture finance. The company has maintained a well-diversified funding profile underpinned by established relationships with lenders and investors, a proactive liquidity management system and a strong credit rating. The company has a diversified base of lenders (including various banks, offshore financial institutions and NBFCs), and investors provide a strong base for increased funding. On the financial front, Northern Arc is among India's diversified NBFCs in terms of AUM as of March 31, 2024, with a business model diversified across offerings, sectors, products, geographies and borrower categories. The company's differentiated credit underwriting processes and risk models have helped deliver strong asset quality. Northern Arc's risk models are supported by a substantial data repository comprising over 35.17 million data points, as of March 31, 2024, on portfolios across multiple sectors assessed throughout the journey and qualitative field-level insights that aid credit assessment and monitoring. According to the CRISIL Report, the company had one of the lowest gross non-performing assets ("GNPA") of 0.45% and net non-performing assets ("NNPA") of 0.08% as of FY24. **The issue is valued at a P/BV of 1.49x on the upper price band based on FY24 book value, which is fairly valued. We, therefore, recommend a Subscribe rating for the issue on the back of a differentiated credit underwriting process, which keeps their asset quality strong and risk-adjusted returns consistent across business cycles.**

Key Risks

- ⇒ The company's operates a diversified business model that exposes them to various risks. An inability to manage such risks may have an adverse effect on the business, results of operations, cash flows, and financial condition.
- ⇒ If the company borrowers' default on their repayment obligations, this may lead to increased levels of non-performing assets (NPA), related provisions, and write-offs and adversely affect the business, results of operations, cash flows, and financial condition.
- ⇒ A significant portion of investments are in credit facilities and debt instruments that are unsecured and/or subordinated to other creditors. An inability to recover such investments may result in increased NPAs, which could adversely affect business prospects, results of operations, cash flows, and financial condition.

Northern Arc Capital Ltd.

Income Statement (Rs. in millions)

Particulars	FY22	FY23	FY24
Revenue from operations			
Interest Income	7,808	11,484	17,121
Interest Expense	4,107	5,574	7,264
Net Interest Income	3,702	5,909	9,857
Fee & commission income	860	856	849
Net gain on fair value changes	426	506	456
Net gain on derecognition	0	203	474
Net Revenue	4,989	7,475	11,637
Other income	70	62	159
Total income	5,059	7,538	11,796
Operating expenses	2,575	4,306	7,584
Employee expenses	979	1,489	2,416
Depreciation and amortization	96	120	169
Other expenses	1,500	2,697	4,999
Operating profit	2,484	3,231	4,212
Provisions	0	0	0
PBT	2,484	3,231	4,212
Tax	665	790	1,025
PAT	1,819	2,422	3,177
Diluted EPS	13.1	17.4	23.4

Source: RHP, BP Equities Research

Cash Flow Statement (Rs. in millions)

Particulars	FY22	FY23	FY24
Cash Flow from operating activities	-13,255	-12,957	-21,345
Cash flow from investing activities	-3,855	-1,195	361
Cash flow from financing activities	20,281	9,280	20,455
Net increase/(decrease) in cash and cash equivalents	3,171	-4,872	-529
Cash and cash equivalents at the beginning of the period	3,981	7,195	2,323
Cash and cash equivalents at the end of the period	7,152	2,323	1,794

Source: RHP, BP Equities Research

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Balance Sheet (Rs. in millions)

Particulars	FY22	FY23	FY24
ASSETS			
Fixed Assets	20	38	67
Loans	52,088	68,886	92,096
Investment	17,658	17,627	17,807
Cash and bank balance	8,025	4,226	4,077
Other assets	1,951	2,938	3,030
Total assets	79,741	93,716	117,077
CAPITAL & LIABILITIES			
Share capital	889	890	894
Reserves & surplus	17,432	18,664	22,317
Net worth	18,321	19,554	23,211
Borrowings	45,994	57,703	76,340
Other liability & provisions	15,426	16,458	17,525
Total Equities and Liabilities	79,741	93,716	117,077

Source: RHP, BP Equities Research

Disclaimer Appendix**Analyst (s) holding in the Stock : Nil****Analyst (s) Certification:**

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