

N R T H E R N A R C

Northern Arc Capital Ltd

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Issue Opens On
Sept 16, 2024

Issue Closes On
Sept 19, 2024

Price Band (INR)
249-263

Issue Size (INR Mn)
7,623-7,770

Rating
SUBSCRIBE

Northern Arc Capital Limited (NACL) was founded in 2009 and offers retail loans to underserved households and businesses in India. Northern Arc Capital's business model is diversified across different offerings, sectors, products, geographies, and borrower categories. As of March 31, 2024, the NBFC has facilitated over INR 1.73 Tn worth of financing, reaching out to over 101.82 Mn people across India. NACL 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 also has an end-to-end integrated technology product suite customized to multiple sectors. This includes an in-house technology stack consisting of (i) Nimbus, (ii) nPOS, (iii) Nu Score, and (iv) Altifi.

OFFER STRUCTURE

Particulars	IPO Details
No. of shares under IPO (Mn)	29.5
Fresh issue (# shares) (Mn)	19.0
Offer for sale (# shares) (Mn)	10.5
Fresh issue (INR Mn)	5,000
Offer for sale (INR Mn)	2,770
Price band (INR)	249-263
Post issue MCAP (INR Bn)	40,436-42,429

Source: IPO Prospectus

Issue	# Shares	INR Mn	%
QIB	14,771,863	3,885.00	50%
NIB	4,431,559	1,165.50	15%
Retail	10,340,304	2,719.50	35%
Net Offer	29,543,727	7,770.00	100%

Source: IPO Prospectus

Indicative Timetable	
Offer Closing Date	Thursday, Sept 19, 2024
Finalization of Basis of Allotment with Stock Exchange	Friday, Sept 20, 2024
Initiation of Refunds	Monday, Sept 23, 2024
Credit of Equity Shares to Demat accounts	Monday, Sept 23, 2024
Commencement of Trading of Eq.shares on NSE	Tuesday, Sept 24, 2024

Source: IPO Prospectus

Objects of the Offer: The net proceeds will be utilized for the following purpose

- Utilize the net proceeds to meet future capital requirements towards onward lending
- Receive the benefits of listing of the equity shares on the stock exchanges, enhancement of its brand name and creation of a public market for equity shares in India.

Shareholding Pattern	Pre-Issue (%)	Post-Issue (%)
Promoters & Promoters Group	0.0%	0.0%
Others	100.0%	100.0%
Total	100.0%	100.0%

Source: IPO Prospectus

Particulars (In INR Mn)*	FY22	FY23	FY24
Net Interest Income (NII)	3,702	5,909	9,857
Net Interest Margins (NIMs)	4.64%	6.31%	8.42%
Pre-Provisioning Operating Profit (PPOP)	2,849	3,623	5,436
Net Profit (after minority interest)	1,725	2,300	3,083
Assets Under Management (AUM)	71,083	90,087	117,100
Net Worth	17,390	19,554	23,143
Return on Average Assets (RoAA)	2.6%	2.7%	3.0%
Return on Average Equity (RoAE)	10.4%	12.6%	14.5%

Source: IPO Prospectus, * Restated Statement, consolidated numbers

Northern Arc Capital Ltd.

Company Overview

Northern Arc Capital Ltd (NACL) 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. Since 2009, NACL's foray into the financial inclusion space has facilitated the financing of over INR 1.73 Tn, positively impacting over 101.82 Mn lives across India as of March 31, 2024.

NACL is one of the leading players amongst India's diversified NBFCs in terms of Assets Under Management (AUM) as of March 31, 2024, with a business model diversified across offerings, sectors, products, geographies and borrower categories. Further, it has one of the lowest industry-wide credit costs amongst diversified NBFCs in India as of March 31, 2024.

NACL has developed domain expertise in enabling credit across its focused sectors in India: Micro, Small and Medium Enterprises (MSMEs) financing, Microfinance (MFI), consumer finance, vehicle finance, affordable housing finance and agricultural finance. The NBFC has been operating in the MSME, MFI and consumer finance sectors for over 14 years, 15 years and nine years, respectively.

NACL serves the retail credit market, including housing finance, vehicle financing, gold loans, education loans, consumer durables, personal loans, credit cards, and microfinance through multiple channels. This includes:

- Extending financing from its balance sheet (Lending) to Originator Partners in the form of loans or investments in Originator Partners debt to enable on-lending to the retail customer (Intermediate Retail Lending) and directly to under-served households and businesses (direct customer Lending) either in collaboration with its Retail Lending Partners or through its branch network to offer rural finance and MSME lending, with AUM of INR 117,100 Mn across 671 districts, 28 states and seven union territories in India, as of March 31, 2024;
- Enabling credit for its Originator Partners through various financing products (Placements), with aggregate Placements volume of INR 1,019,039 Mn, as of March 31, 2024, and
- Managing debt funds and providing portfolio management services (Fund Management), with aggregate fund deployed of INR 120,786 Mn across 10 Alternate Investment Funds (AIFs) and three Portfolio Management Service (PMS) funds, as of March 31, 2024.

NACL has built an efficient and scalable business model, supported by its proprietary end-to-end integrated technology product suite customized to multiple sectors.

The NBFC's in-house technology stack consists of: (i) Nimbus, a curated debt platform that enables end-to-end processing of debt transactions; (ii) nPOS, a co-lending and co-origination technology solution based on Application Programming Interfaces (API); (iii) Nu Score, a customized machine learning based analytical module designed to assist its Originator Partners in the loan underwriting process; and (iv) Altifi, an alternative retail debt investment platform.

The NBFC serves the retail lending market through a multi-channel approach that includes:

➤ Lending:

- NACL is a systemically important non-deposit taking Non-Banking Finance Company registered with the RBI. From its balance sheet, the NBFC extends financing in the following manner:
 - a) **Intermediate Retail Lending:** NACL lends to and guarantees the borrowings of its large network of financial institution partners, technology platforms (such as financial technology businesses (Fintechs)) and other entities that act as business correspondents to originate financial exposure (collectively, Originator Partners). The NBFC finances Originator Partners through various methods depending on the specific needs of each partner, such as:
 - lending to and investing in debt securities issued by Originator Partners primarily for the purpose of retail on-lending by them. Such products include loans, Non-Convertible Debentures (NCDs), market-linked debentures and Commercial Papers (CPs).
 - providing guarantees for borrowings by Originator Partners; and
 - investing in retail portfolios originated by Originator Partners through portfolio financing transactions such as rated securitization and direct assignment.
 - b) **Direct to Customer Lending:** NACL provides loans directly to underserved households and businesses, such as MSMEs, MFIs, and consumers in the vehicle finance sector, using a "phygital" approach. This approach combines technology platforms and a data-first strategy with a network of 316 physical branches across India and 50 select Originator Partners. These partners enable the NBFC to lend directly to its customers, providing services such as loan origination, KYC verification, loan servicing, data collection, borrower interface, collections, recoveries, customer service, and grievance redressal as of March 31, 2024. Its rural financing business, operated through its subsidiary Pragati, serves as the business correspondent for the direct rural financing business. In addition, the company provides technology-enabled supply chain financing and secured MSME lending. These initiatives have demonstrated scalability and allowed the NBFC to effectively reach out to Direct-to-Customer Borrowers in remote areas at the last mile.

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> Placements:

- NACL utilizes the Nimbus technology platform to collaborate with a diverse group of investors representing various investor classes. These investors leverage NACL as a means to explore investment opportunities in underserved sectors in India. This includes participation in placements, structured and syndicated financing, debt instruments, credit-enhanced debt, and portfolio financing products.
- Furthermore, NACL provides credit enhancements and co-investment options in transactions to attain the desired credit rating and offer assurance to its investor partners, setting it apart from other market facilitators.

> Fund Management:

- NACL's Fund Management channel is operated through its subsidiary, NAIM. Based on contributions received from Investor Partners, NAIM manages debt funds that invest largely in the sub-set of Originator Partners and mid-market companies in line with the investment mandate of the respective funds.
- The NBFC has also made capital contributions to the funds managed by NAIM, in addition to the sponsor contribution by NAIM in each of its funds. In August 2021, NAIM obtained its registration as a portfolio manager from SEBI to conduct PMS and launched its first PMS fund in FY23.
- As of March 31, 2024, NACL had raised INR 37,450 Mn in investor commitments across 10 AIFs and three PMS funds, out of which it has facilitated successful exits for Investor Partners in four AIFs and one PMS fund.

The following table presents the breakdown of NACL's Gross Transaction Volume (GTV) by sector for the indicated FYs:

Sectors	FY22		FY23		FY24	
	Amount (INR in Mn)	% of total	Amount (INR in Mn)	% of total	Amount (INR in Mn)	% of total
MSME	70,764	35.6%	76,078	27.8%	81,609	27.8%
MFI	52,659	26.5%	81,338	29.7%	76,230	26.0%
Consumer Finance	32,067	16.1%	85,743	31.3%	101,175	34.5%
Vehicle Finance	34,636	17.4%	20,761	7.6%	19,013	6.5%
Affordable Housing Finance	4,797	2.4%	6,633	2.4%	10,155	3.5%
Agriculture Finance	4,041	2.0%	3,300	1.2%	5,056	1.7%
Total GTV	198,964	100.0%	273,852	100.0%	293,237	100.0%

Source: IPO Prospectus

• MSME:

- NACL extends loans to under-served MSME businesses and NBFCs engaged in MSME financing either directly or through its Originator Partners. This sector offers diverse funding opportunities across various industries, determined by the performance and potential of the businesses. It facilitates debt financing for purposes including secured and unsecured small business lending, merchant financing, supply chain financing, school financing and support for micro and medium-sized corporations.

• Microfinance (MFI):

- NACL offers microfinance loans to under-served individuals, either directly through its dedicated rural finance partner subsidiary, Pragati, acting as its business correspondent, or in collaboration with its Retail Lending Partners and Originator Partners. The NBFC's primary focus in microfinance is the Joint Liability Group (JLG) lending format, wherein borrowers form groups and share responsibility for each other's loan repayments in case of default, providing social collateral.

• Consumer Finance:

- NACL extends financing to individuals from new to credit backgrounds and other under-served categories, encompassing employed and self-employed individuals, either directly or by collaborating with Originator Partners, many of whom eventually become its Retail Lending Partners. NACL offers a variety of consumer finance solutions, including consumer durable loans, cash or personal loans, salary advance loans, and buy-now-pay-later financing for products and services available through both online and offline channels.
- In addition, NACL's Originator Partners and Retail Lending Partners in this sector offer various digital consumer payment services, such as checkout financing and personal loans.

• Vehicle finance:

- NACL primarily works with Originator Partners operating in the vehicle sector, who enable to lend to under-served individuals and businesses exploring financing for the purchase of commercial vehicles used for commercial transportation of goods or passengers, two-wheelers, Electronic Vehicles (EV) as well as companies engaged in e-mobility, EV fleet services, EV infrastructure (battery swapping) and EV last-mile delivery.

• Affordable housing finance:

- NACL works with Originator Partners, mostly being Housing Finance Companies (HFC), who lend to self-employed or salaried borrower categories for the purchase of residential property, home improvement and home extension.

• Agriculture finance

- NACL works with Originator Partners, providing post-harvest services and financing in the agricultural and allied sectors. This includes players who provide commodity warehousing services and warehouse receipt financing, as well as players who finance agricultural and allied activities, often working through aggregators such as farmer-produce organisations or dairy cooperatives.

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Industry Overview

Credit penetration in India

- The retail credit (including Housing finance, Vehicle Financing, Gold Loans, Education Loans, Consumer Durables, Personal loans, Credit cards and Microfinance) in India stood at INR 75.2 Tn as of FY24 and has rapidly grown at a CAGR of 16.0% during FY20 and FY24.
- In FY23, retail credit has grown at ~22.3% YoY. The Indian retail credit market has grown at a robust pace over the last few years and is expected to further grow at a CAGR of 17.0-18.0% between FY24 and FY26E to reach INR 100.9 Tn by FY26E.
- The moderation of growth of retail credit is on account of normalization in an unsecured segment, which had witnessed exuberant growth in the past and the impact of RBI's risk weight circular.
- The increasing demand and positive sentiments in the Indian retail credit market present an opportunity for both banks and NBFCs to broaden their investor base.

Personal Loan and Service segment to drive credit growth in FY25E:

- The agricultural credit in FY24 is estimated to be grown due to higher Priority Sector Lending (PSL) targets, expected higher food-grain production, an increase in commodity prices and an increase in agriculture credit target.
- The services segment grew in FY24 on the back of healthy credit demand from Non-Banking Financial Companies (NBFCs).
- The personal Loans segment grew in FY24, driven by a sharp rise in demand for unsecured loans, demand in the housing segment and pent-up demand in the vehicle loans segment.
- Going forward, the personal loans and services segment is expected to drive credit growth in FY25E. The personal Loans segment is expected to show strong growth in FY25E on the back of credit demand from consumer durables, gold and another personal loan segment.

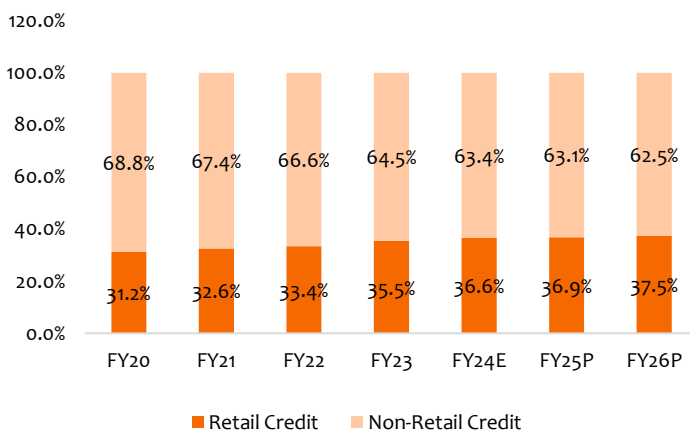
Housing finance accounts for third highest share in overall NBFC credit as of FY24:

- As of FY24, infrastructure financing accounts for the highest share of NBFC credit (24.0%), followed by MSME loans, which account for a 21.0% share of overall NBFC credit.
- Housing finance accounted for the third highest share in overall NBFC credit outstanding, with a 16.0% share in overall NBFC credit.
- Housing finance accounted for the highest share in NBFC retail credit across fiscals, accounting for 36.0% as of FY24, and witnessed a fall in share from 41.0% in FY20. This was followed by vehicle financing and personal loans with 32.0% and 15.0% share in FY24, respectively.

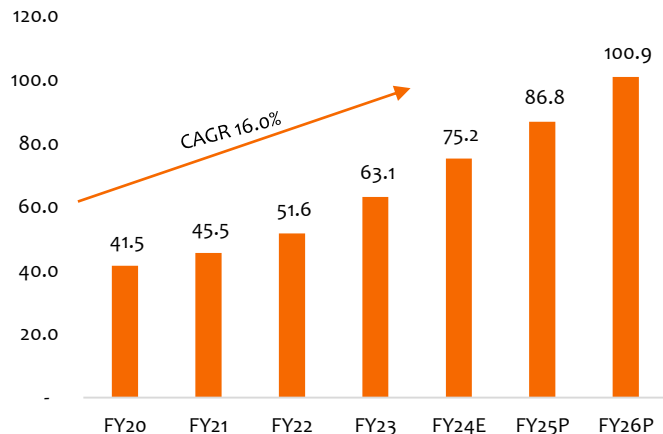
Digital payments have witnessed substantial growth:

- Between FY18 and FY24, the volume of digital payment transactions increased from INR 14.6 Bn to INR 164.4 Bn, causing its share in overall payment transactions to increase from 59.0% in FY18 to 97.0% in FY24.
- During the same period, the value of digital transactions increased from INR 1,371 Tn in FY18 to INR 2,428 Tn in FY24.
- Consumers are increasingly finding transacting through mobile convenient. The share of mobile banking and prepaid payment instruments is expected to increase dramatically over the coming years.
- In addition, improved data connectivity, low digital payment penetration and proactive government measures are expected to drive digitalization in the country, transforming it into a cashless economy.

Retail segment to account for 37.5% of overall systemic credit by FY26E



Retail credit growth to continue a strong footing in FY25P and FY26P (INR in Tn)



Source: IPO Prospectus; Note: E- Estimates; P- Projected

Northern Arc Capital Ltd.

Industry Overview

Account aggregators

- The RBI launched the Account Aggregator (AA) system on September 2, 2021. This has the potential to transform the financial landscape once there is widespread adoption amongst the stakeholders.
- AAs are essentially non-banking financial companies licensed by RBI that act as an intermediary to collect and consolidate data from all Financial Information Providers (FIPs), such as banks, that hold users' personal financial data and share that with Financial Information Users (FIUs), such as lending agencies or wealth management companies that provide financial services.

NBFC credit to grow faster than systemic credit between FY24 and FY26E:

- NBFC credit is expected to grow at 16.0%-18.0% between FY24 and FY26E. The credit growth will be driven by the retail vertical, including housing, auto, and microfinance segments.
- The organic consolidation is underway, with larger NBFCs gaining share with some of the mergers and acquisitions in the NBFC space, such as Ambit Finvest's acquisition of SME Corner and the merger of Incred and KKR India.
- Further growth of the NBFC industry will be driven mainly by large and medium-sized players with strong parentage who have funding advantages and the capability to invest and expand into newer geographies.

Retail segment to support NBFCs overall credit growth:

- Going forward, growth in the NBFC retail segment is expected at 16.0-18.0% CAGR between FY24-FY26E which will support overall NBFC credit growth, with continued focus on the retail segment and multiple players announcing plans to reduce wholesale exposure.
- The retail segment's market share is expected to rise further to 48.0% by end of FY25E and remain around 48.5% in FY26E.

Impact of digitization on retail credit:

- Digital lending products such as instant loans or online personal loans have completely revolutionized retail credit due to great convenience that it offers to the customers.
- The India Stack, a set of APIs and tools that enable the building of digital platforms for various services, has been a game-changer in the retail credit sector.
- Looking ahead, the digitization of retail credit in India is expected to continue evolving.

Securitization asset pool getting wider with emergence of newer asset classes:

- Mortgages share has reduced over the course on account of non-participation of few large mortgage loan originators who were active participants previously.
- Relatively newer asset classes, such as car-lease and supply-chain receivables, were also seen getting securitised last fiscal.
- While traditional asset classes like mortgage loans, commercial vehicle loans, construction equipment loans and micro finance loans continue to dominate the structured finance space, the market has also seen noticeable innovation over the past few years with new structures being introduced that has helped expand the market.

Opportunities in partnership-based lending:

- Partnership Based Lending (PBL), or Co-Lending Model (CLM), refers to an arrangement between two parties wherein one of the parties agrees to take over a larger proportion of the loan (usually 80.0% in PBL and 100% in case of loans originated by business correspondents) originated by another party on its books, with the originator taking on the remaining (usually 20.0% in PBL) on its books.
- CLM is operationally convenient for both partners as it enables partners to offer multiple products to customers who are not otherwise present in their current portfolio, thus providing diversification to the portfolio without having a separate operational setup for each product. Co-lending, therefore, enhances operating leverage for financiers, enabling them to increase lending with existing infrastructure and resources.
- Entering into CLM allows smaller NBFCs to cater to a larger customer base with lesser capital by leveraging their partners' larger balance sheets. Such NBFCs can leverage their origination skills and expertise in assessing specific customer segments while at the same time conserving their capital.

Growth drivers of AIF Industry in India:

- GIFT City AIFs have several preferential rules concerning single window clearance, leverage, diversification restrictions, the absence of SEBI approval for investments outside India, and deal structuring and capital allocation.
- Category III AIFs with foreign investment are permitted to make portfolio investments in only those securities or instruments in which an FPI (Foreign Portfolio Investor) can invest under the Foreign Exchange Management Act, rules or regulations made thereunder.
- IFSC has permitted higher leverage levels for Category II funds with the consent of the fund's investors. Additionally, the IFSC has offered flexibility to fund the managers and investors with regard to co-investment and diversification norms for fund portfolios.

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Strengths:

Large addressable and underpenetrated market with strong sectoral expertise:

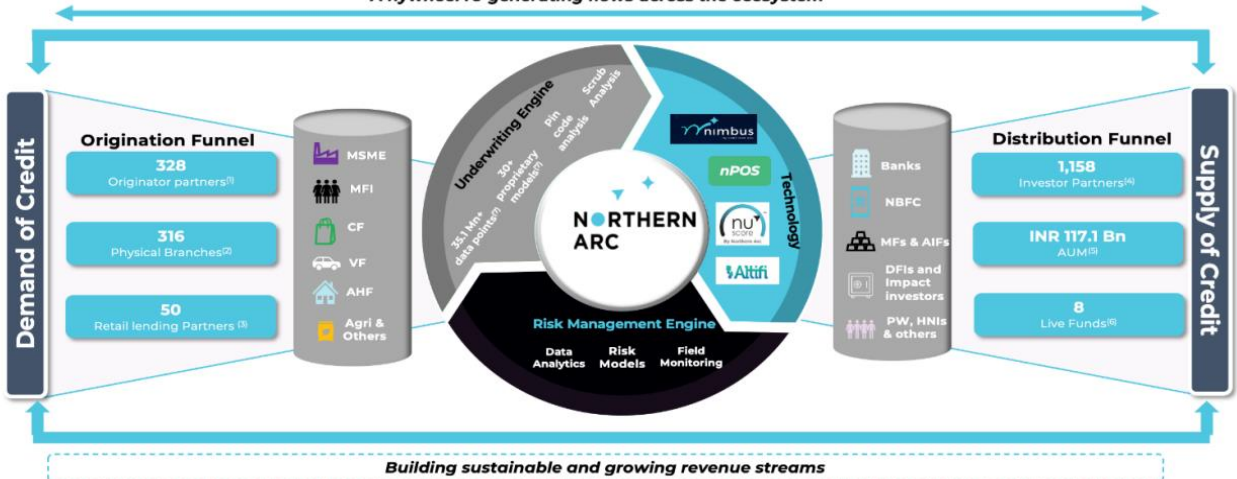
- In terms of the credit-to-GDP ratio, India has a low credit penetration compared with other developing countries, such as China, indicating a significant untapped potential.
- Rural areas, which accounted for 47.0% of GDP, received only 9.0% of the overall banking credit as of March 31, 2024, which also shows the vast market opportunity for banks and NBFCs to lend in these areas.
- Government initiatives such as Pradhan Mantri Jan-Dhan Yojana (PMJDY), Aadhaar, and widespread digitization (referred to collectively as the 'JAM Trinity') have expanded the formal financial inclusion for underserved Indian population.
- The widespread availability of affordable data and digital disruption has transformed the financing landscape in India.
- 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.
- The Indian retail credit market has grown at a robust pace over the last few years and is expected to further grow at a CAGR of 17.0-18.0% between FY24 and FY26E to reach INR 100.9 Tn by FY26E. Thus, NACL believes this presents the NBFC with an opportunity to capitalize on the large potential for growth in the retail credit market, particularly in rural and semi-urban areas.
- By leveraging its diversified business model and proprietary technology product suite customized to multiple sectors, NACL has, over the last 15 years, developed strong sectoral expertise in enabling credit across its focused sectors: MSME, MFI, consumer finance, vehicle finance, affordable housing finance and agriculture finance.
- The NBFC has strengthened its retail MSME outreach by introducing Loan Against Property (LAP) financing in FY22 and supply chain finance in FY23. The LAP financing provides secured business loans directly to MSMEs through 50 branches as of March 31, 2024.
- NACL's technology-driven supply chain financing business offers financing solutions to various participants within the enterprises' supply chain network.
- The NBFC offers a comprehensive portfolio of products and services in the consumer finance sector, including consumer durable loans, cash or personal loans, salary advance loans, and buy-now-pay-later financing through both online and offline channels in collaboration with its Retail Lending Partners.

Large ecosystem of partners and data and technology platform creating strong network effects:

- Over the past 15 years, NACL has been a key player in the Indian retail credit market, enabling the financing of over INR 1.73 Tn since 2009. This has positively impacted more than 101.82 Mn lives and fostered a network of 328 Originator Partners, 50 Retail Lending Partners, and 1,158 Investor Partners as of March 31, 2024.
- NACL offers multi-channel services, including Lending, Placements, and Fund Management, supported by proprietary technology solutions and a substantial data repository of over 35.17 Mn data points as of March 31, 2024.
- This large and growing community of Originator Partners, Retail Lending Partners and Investor Partners coupled with its track record in diversified product offerings and the proprietary technology stack, has resulted in an expansion in its opportunities for debt raising and investment.
- This helps access large pools of liquidity, serves wider classes of investors, and meets their varied requirements.
- This generates an annuity effect, providing a combination of fee income and interest income. Accordingly, this creates positive network effects and a scalable and diversified platform.

Multi-channel approach that has impacted over 101.82 million⁽⁷⁾+ lives across focus sectors through a 'digital & data first' approach

A flywheel re-generating flows across the ecosystem



Source: IPO Prospectus

Northern Arc Capital Ltd.

Strengths:

- NACL's Lending channel utilizes a credit underwriting framework to discover and support Originator Partners that are customer-focused, committed to meeting the credit needs of underserved segments, and have the potential for growth through debt access.
- Most of its Originator Partners are initially relatively smaller in scale and typically have limited avenues of raising debt. This allows NACL to build long-term relationships with first mover advantage and benefit from continued engagement as they scale up their businesses and grow their credit requirements.
- NACL also partners with Retail Lending Partners to lend to Direct-to-Customer Borrowers, who provide NACL with the necessary support in various functions such as loan origination, execution of loan documents, disbursements and collections.
- NACL has also built partnerships with Investor Partners across different investor classes, including banks, asset management companies, insurance companies, DFIs, fund-of-funds, AIFs, Foreign Portfolio Investors (FPIs), global investment vehicles, family offices, private wealth managers, foundations and HNIs, who access opportunities to invest in the under-served households and businesses in India through its platform.
- NACL's technology products and data capabilities are the backbone of its ecosystem, which ensures the seamless interaction between Originator Partners and Retail Lending Partners as well as Investor Partners, facilitated through its technology platform, Nimbus, that enables end-to-end processing of debt transactions.
- To deepen its relationships with Originator Partners, NACL has developed a proprietary technology product, Nu Score, a tailored machine learning-based scoring module designed to assist its Originator Partners in the loan underwriting process and help them make effective credit decisions.
- NACL has developed nPOS, a fully integrated API-based technology solution that seamlessly integrates with the systems of Originator Partners (including Retail Lending Partners) and Investor Partners, easing the co-lending process.
- AltiFi, NACL's alternative retail debt investment platform, further enables it to capture a broader base of retail investors, who may subsequently graduate to investing in its funds.

Proprietary technology product suite transforming the debt market ecosystem:

- NACL is a technology-driven financial services platform supported by in-house technology solutions and architecture, driving a scalable and sustainable business model that enables it to expand and scale its business and drive growth in revenue.
- Nimbus provides the ability for end-to-end processing of debt transactions, from loan application, credit evaluation, and generation of legal documentation to transaction execution and closure, leading to distinct advantages for the users, such as scale, precision, transparency and efficiency in turnaround time.
- Nimbus covers the full spectrum of internal functions ranging from partner onboarding, credit evaluation and decisions, approval of credit exposure limits, data-driven risk monitoring and analytics, documentation and execution, to post-transaction compliance and monitoring.
- In FY24, the number of active Originators Partners and Investor Partners on Nimbus was 147 and 72, respectively. As of March 31, 2024, NACL has enabled credit of INR 997.16 Bn through Nimbus.
- nPOS is configurable and provides a streamlined process for partnership-based loan origination, underwriting, disbursement, and collection reconciliation.
- In FY4, the number of active partners and value of transactions on nPOS was 21 and INR 59,891 Mn, respectively. Further, nPOS received the 'Best Lending Fintech Platform' award at the 4th edition of the Smart CX Summit & Awards in May 2024.
- AltiFi offers secondary sales of corporate bonds that have been assessed for its investments, public issuances of bonds and primary issuances of sovereign gold bonds.
- As of March 31, 2024, AltiFi had 30,518 registered users sourced directly and, with the help of distributors who have, on aggregate, enabled over INR 4,163 Mn of investments. This end-to-end digital platform democratizes debt securities on its balance sheet for investment opportunities to retail individuals and corporates.
- A single metric (Nu Score) provides a comprehensive view of borrower parameters, facilitating informed lending decisions and aiding financial inclusion. In FY24, the number of assessments conducted through Nu Score was 17,052.

Robust risk management based on domain expertise, proprietary risk models and data repository driving asset quality:

- NACL leverages its expertise and data to develop customized and proprietary risk models that suit its offerings, products and markets and enhance its capital efficiency.
- Most of its credit risk management processes are enhanced through deep analytical models built on Nimbus, which leverages internal and external data sources to create in-depth risk analytics and modelling. It also has early warning systems that help proactively deal with and minimize risks.
- NACL adds insights from its on-field surveillance to Nimbus to allow for a comprehensive data repository.
- It obtains and periodically updates the credit information of its customers by checking the credit bureaus, which are used in pool selection and building its financial models.

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Strengths:

- As of March 31, 2024, NACL conducted reviews on 677 Originator Partners, out of which the NBFC performed due diligence on 430 Originator Partners and successfully onboarded 328 Originator Partners onto its platform.
- The NBFC has developed over 30 analytical models as of March 31, 2024, using the data repository and insights from its on-field surveillance and continuously strengthening them by adding more data points and sources.
- NACL's diversified presence across India mitigates the impact of any adverse geography-specific risk events, including natural disasters.
- The sectoral diversification has helped NACL mitigate the effects of slowing demand for credit in standalone sectors owing to cyclicity, events or regulatory changes affecting such sectors and maintaining the health of its portfolio, resulting in lower risk, return and growth volatility.
- NACL has developed a comprehensive collection capacity (comprising an in-house call center, its team and empaneled agencies for field collections and field collections teams), which, together with pre-default early alerts, enables risk control and maximizes post-default recoveries of its exposures.
- NACL had one of the lowest GNPA of 0.45% and NNPA of 0.08% as of FY24.

Particulars	FY22	FY23	FY24
Gross Stage 3 – Loans and Investments (%)	0.50%	0.77%	0.45%
Net Stage 3 (%)	0.21%	0.40%	0.08%
NBFC's GNPA ratio (%)	5.80%	5.00%	4.10%
NBFC's NNPA ratio (%)	2.30%	1.70%	1.50%

Source: IPO Prospectus

Diversified sources of funding for its own deployment and proactive liquidity management:

- NACL has maintained a well-diversified funding profile that is underpinned by its established relationships with its lenders and investors, proactive liquidity management system and strong credit rating.
- The NBFC's diversified base of lenders (including various banks, offshore financial institutions and NBFCs) and investors provide a strong base for increased funding.

Type of Lenders	FY24		
	Number of lenders	Amount (INR in Mn)	% of total
Banks	31	61,457	67.9%
Domestic DFIs	1	3,864	4.3%
Offshore Financial institutions	6	14,404	15.9%
NBFCs	7	8,183	9.0%
Domestic capital markets	0	0	0.0%
Domestic retail/ HNIs	4	2,569	2.8%
Total Borrowings	49	90,478	100.0%

Source: IPO Prospectus

- NACL's credit rating was also upgraded to AA- (Stable) credit rating by ICRA and India Ratings in March 2023 and September 2023, respectively, from A+ credit rating for all of its long-term facilities and non-convertible debentures, respectively.
- ICRA further reaffirmed the AA- (Stable) credit rating for all its long-term facilities and non-convertible debentures in July 2024.
- The NBFC's NCDs and long-term bank facilities are rated AA- (Stable) as rated by ICRA in March 2023 and re-affirmed in September 2023, March 2024 and July 2024.
- NACL has been able to service its debt obligations during challenging industry and macroeconomic events and credit cycles for NBFCs.
- The NBFC has demonstrated the ability to improve its borrowing costs, even in environments characterized by rising interest rates in recent years.
- The NBFC has adopted an asset/ liability management policy that requires NACL to monitor and manage interest rate and liquidity risks from time to time.

Particulars	FY22	FY23	FY24
Average tenure of borrowings (years)	3.03	3.38	3.07
Incremental cost of borrowing (%)	8.45%	9.48%	9.48%
Average Cost of Borrowing (%)	8.55%	8.84%	9.23%

Source: IPO Prospectus

Northern Arc Capital Ltd.

Strengths:

Professional management team supported by an experienced Board and marquee investors driving high standards of Governance:

- NACL has an experienced leadership team has played a pivotal role in building its business and brand.
- The NBFC's Directors, Key Management Personnel and Senior Management have substantial experience in the banking, financial services and insurance (BFSI) space in both India and abroad.
- The team of Key Management Personnel and members of its Senior Management have been with its NBFC for an average of more than five years.
- The NBFC strives to adhere to high corporate governance standards and has established policies and procedures to support transparency, strong business ethics and a well-established compliance framework.
- The Board is chaired by a Non-Executive Independent Director, with three additional Non-Executive Independent Directors, three Non-Executive Nominee Directors, one Non-Executive Non-Independent Director and one Managing Director.
- The NBFC aims to be an equal-opportunity employer focusing on diversity and nurturing women's talent.
- NACL has endeavored to motivate its senior and mid-level management team through a combination of variable compensation linked to individual performance and its performance and long-term incentives.

Strong ESG framework integrated into the business model with focus on creating sustainable impact and climate-smart lending:

- NACL enforces ESG parameters as part of its corporate governance commitment to its shareholders, including through adherence to the LeapFrog Group's 'Responsible Investment Code', to deliver financial and social results by incorporating best practices across environmental, social and governance impact management.
- As of December 31, 2023, more than 43.96% of the total underlying borrowers of its Originator Partners comprised women. In addition, as part of its ESG policy, NACL looks into whether its customers meet certain minimum standards of corporate governance.
- Given its historical and overarching focus on enabling access to finance for under-served households and businesses, NAIM manages funds focusing on social impact.
- As of March 31, 2024, NACL's AUM to Originator Partners, which is directly attributable to addressing climate adaptation, mitigation, and action, was INR 763 Mn.
- In response to the increasing importance of climate-focused financing, NACL also provides funding to Originator Partners in the EV financing sector and mid-market companies engaged in e-mobility, battery manufacturing, solar power projects, EV fleet services, EV infrastructure (battery swapping) and EV last-mile delivery, with the primary goal of reducing carbon emissions.

Northern Arc Capital Ltd.

Future Growth Strategies

Enhance its ecosystem by growing and deepening relationships with its partners, while leveraging and scaling up the technology products:

- NACL plans to expand its footprint to better reach and serve underserved households and businesses in its focused sectors in India by:
 - adding to and strengthening its origination channels, i.e., by on-boarding new Originator Partners onto its platform and financing the debt capital requirements for the growth of its Originator Partners, and on-boarding new Retail Lending Partners who can help us reach more Direct to Customer Borrowers; and
 - increasing the use of and scale and leveraging its in-house technology and data-enabled products and platforms.
- NACL believes that existing investor partners will diversify their product and investment portfolios as their deployment requirements grow and its understanding of its focused sectors deepens. This will help NACL enhance financing volumes across its channels and further widen the impact on the end borrowers.
- NACL's continued focus on the effective use of technology is aimed at further improving the customer experience and streamlining processes, including loan origination, credit underwriting, risk management, collections, customer service and retention, leading to cost efficiencies and productivity.
- NACL plans to further leverage its data solution, Nu Score, to enhance the underwriting process for its Originator Partners, which would promote deeper integration within its partner ecosystem.
- The NBFC plans to add more products on its AltiFi platform to offer full-scale wealth management services comprising products across savings, investments (such as listing of commercial papers, fixed deposits and mutual funds) and insurance, which NACL believes will help in broadening the coverage of retail investors as well.

Expand to adjacent sectors such as climate lending and gold loans, and enhance its ESG risk management systems:

- NACL intends to identify incremental opportunities across sectors and within sectors across products. In particular, it plans to explore opportunities to participate directly and collaborate with its Originator Partners in the climate and sustainability sector.
- The NBFC aims to work with environmentally conscious organizations in the MSME sector to create climate-neutral products such as electric mobility and allied solutions, solar energy harvesting and distribution, and waste recycling and financing sustainable water and sanitation solutions.
- The EV industry and its financing are experiencing significant growth due to the escalating focus on climate change and sustainability. NACL also aims to partner with DFIs to create thematic funds on climate financing and work with various stakeholders to design products and mobilize funds for such underlying sectors.
- The gold loans AUM is expected to grow at 14.0-15.0% CAGR between FY24 and FY27E to reach INR 11,307 Bn by March 2027 (E). NACL intends to enter the gold loan sector through existing and new originator partners. The NBFC aims to transition these Originator Partners into Retail Lending Partners to directly serve borrowers in this sector and thereby build a granular loan portfolio.
- NACL aims to upgrade its existing ESG risk management system by including screening, categorization, and due diligence procedures, additional studies if required, guidance on certain debt structures/investments with potentially limited leverage, monitoring of the portfolio and use of external consultants for due diligence.

Expand its Fund Management channel:

- NACL is focused on capitalizing on its innovative products, track record of returns, and established investor base to deepen its offerings further and scale its business.
- The NBFC intends to launch thematic funds targeting climate, agriculture, financial services and gender. Further, it is also focused on expanding the focus of its funds.
- NACL aims to launch interval funds and custom corporate-focused yield/ tenor funds targeted towards retail and corporate investors for its PMS offering.
- In addition to its current Mauritius fund, NACL has and intends to continue to grow its presence in the International Finance Services Centre (IFSC) located in Gujarat International Finance Tec-City (GIFT City) by aiming to launch various funds including a climate-focused fund.
- NACL aims to increase its investor base by targeting new investors, particularly in Asia, and deepen its relationships with its existing European and United States investor base.
- In India, NACL's PMS funds have onboarded both corporates and smaller ticket investors through independent financial advisors, and its new fund launches are aimed at broadening this investor category.

Continue to scale its Direct to Customer Lending channel to enhance risk adjusted returns:

- NACL has and continues to be focused on expanding its Direct to Customer Lending channel in order to capitalize on the growing retail credit market in India.
- NACL intends to continue to expand its 'phygital' presence by leveraging its proprietary and differentiated technology infrastructure and underwriting and risk management capabilities.

Northern Arc Capital Ltd.

Future Growth Strategies

- NACL aims to leverage its rural finance network, which provides unsecured small-ticket loans to rural borrowers, by introducing new products and giving larger-value loans to these borrowers as they go through their credit life cycle.
- The NBFC intends to capitalize on its technology and data-first philosophy to foster growth and productivity in India's underserved rural and semi-urban areas.
- It intends to focus on funding small businesses directly by expanding and diversifying its product portfolio.
- NACL aims to offer comprehensive financial solutions, including term loans, structured working capital, secured loans backed by property collaterals and supply chain finance, that provide holistic support to MSMEs and cater to their various needs.

Focus on credit quality to manage credit cost efficiently:

- NACL's customer-centric approach is pivotal in effectively managing customers throughout their life cycle.
- The incorporation of predictive, data-driven decision-making enables NACL to anticipate and respond to customer actions in real-time, thereby streamlining the efficient management of credit costs.
- The NBFC aims to continue to focus on improving its credit quality through its 'credit first' approach to manage its credit costs more efficiently.
- NACL intends to continue to invest, build and enhance incremental risk monitoring, analytical and collection capabilities across functions and increase the deployment of machine learning techniques to deepen its data repository to identify and address early alert credit risk events in its portfolio as well as those of its partners.
- NACL believes that the extensive usage of its data models and technology products will enable the development of a comprehensive framework for efficient credit cost management.

Continue to diversify its source of funds and widen the lender base to scale the borrowing requirements while lowering costs:

- NACL has been and continues to be dedicated to diversifying its borrowing profile, optimizing borrowing costs, creating sell-down opportunities and maintaining a positive ALM position.
- Low borrowing costs are crucial for competitively pricing its loan products, driving business growth towards the desired asset quality for the portfolio, increasing risk-adjusted margins and maintaining a strong market position.
- The NBFC intends to continue to diversify its lender base, enhance limits from existing sources, identify new sources and pools of capital and strengthen asset liability management policies further, aiming to further optimize its borrowing costs.
- It aims to prioritize long-term borrowing to ensure stability and maintain liquidity risk in line with its ALM approach.
- With NACL's continued focus on increasing its direct-to-customer lending, the NBFC's ability to sell down in direct assignment will also continue to grow. As of March 31, 2024, its sell-down exposures through direct assignment were INR 7,766 Mn.

Expansion through inorganic growth:

- NACL intends to maintain and increase its position as a leading platform in the financial ecosystem through inorganic growth opportunities.
- NACL may, from time to time, evaluate and pursue strategic acquisitions, alliances, partnerships and joint ventures, including portfolio acquisitions.
- The NBFC's expansion will be driven by opportunities to grow its revenues by tapping into new opportunities in its existing and new markets.

Northern Arc Capital Ltd.

Key Risks

- The diversification, size and complexity of business and operations subjects NACL to various risks relating to, amongst others, credit, liquidity, market (including interest rate, foreign currency, price), operational, technology, regulatory and compliance, reputational and strategic, some of which is outside its control.
- Through the Lending channel, NACL either extend loans to its Direct-to-Customer Borrowers or extends loans to and invests in the debt of its Originator Partners for retail on-lending by them. As a result, NACL is vulnerable to default risks from these borrowers and, along with its Originator Partners, to the borrowers, Originator Partners, on-lend the financing availed from NACL.
- The NBFC has no identifiable promoter in terms of the SEBI ICDR Regulations and the Companies Act 2013. Accordingly, the success of its business operations depends on its senior management team and key management personnel, as well as its ability to attract, train and retain such employees.
- A significant portion of its investments are in unsecured credit facilities and debt instruments and/or subordinated to other creditors. An inability to recover such investments may result in increased levels of NPAs, which could adversely affect the business, prospects, results of operations, cash flows and financial condition.
- In 2017, NACL was issued an administrative warning by SEBI due to its use of Sharepro Services (I) Private Limited as the Registrar and Share Transfer Agent for its securities and its failure to comply with SEBI's order to transition operations from Sharepro. NACL terminated its services with Sharepro and appointed a new RTA in October 2016. Any future non-compliance by NACL with rules and regulations may result in penal actions, such as restrictions on further issuance of securities and freezing of transfer of securities, which could negatively impact the company's business, operations, cash flows, and financial condition.
- The NBFC operates in a highly competitive industry, and its inability to compete effectively may adversely affect its business and reputation.
- NACL's inability to raise further credit facilities, collect sufficient cash from borrowers as per the scheduled maturity period or renew its existing facilities in a timely and cost-effective manner or at all may lead to mismatches in its assets and liabilities, which in turn may adversely affect the operations, financial performance and cash flows.
- The capital and lending markets, particularly debt and money markets, are highly volatile, and prevailing economic conditions could adversely affect NACL's access to liquidity.
- The NBFC's premises are either leased or on a seat-sharing basis. Non-renewal or dispute with lessor or co-tenants may lead to disruption of business and cost associated with shifting its offices, which may hurt the company.
- Negative cash flows over extended periods or significant negative cash flows in the short term may materially impact NACL's ability to operate the business and implement its growth plans.
- A natural disaster, severe weather conditions or an accident that damages or otherwise adversely affects any of its business operations or its customers' business operations or livelihood could have a material adverse effect on the business, financial condition, cash flows and results of operations.

Northern Arc Capital Ltd.

Outlook and Valuation

Northern Arc Capital Ltd (NACL) has built a solid foundation supported by its expansion in business, strong alliances, and efficient operations. Consequently, the NBFC has experienced a strong 33.7% CAGR growth in its Profit After Tax (PAT) and a 38.1% CAGR growth in operating profit from FY22 to FY24. NACL is focused on establishing a future-ready organization that offers customers convenient and cost-effective solutions by automating a considerable portion of its current business operations. The way NACL has set up its organization, invested in new capabilities, and pursued data and digital initiatives has been strategically planned to drive its upcoming growth phase. Favorable macroeconomic conditions, regulatory stability, and an improved operating environment support the promising prospects of the NBFC sector. Well-capitalized companies such as NACL, with robust provisioning norms and sufficient liquidity, are well-positioned to outperform the industry in the near future. Asset classes such as microfinance, MSME finance, housing loans, and vehicle finance are expected to see increased demand. Moreover, consumer loans such as personal and gold loans are projected to gain traction, which is advantageous for NACL. The NBFC plans to utilize the net proceeds from its recent INR 5,000 Mn issue to strengthen its capital base and expand its lending capabilities.

At the upper end of the price band, NACL's price-to-book value multiple stands at 1.5x for the post-IPO book value of INR 174.5 per share as of March 31, 2024 (FY24), which is reasonable compared to its peers. The average price-to-book value for the peers is 3.5x. We have a positive outlook on NACL's future as it is strategically enhancing its ecosystem through cultivating and strengthening partnerships while expanding its technology products to improve customer experience and operational efficiency. Additionally, the company is diversifying into new sectors, which presents exciting growth opportunities. Therefore, we recommend rating Northern Arc Capital Ltd.'s IPO as 'SUBSCRIBE'.

Peer Comparison

Comparison with listed industry peers (FY24)

Name of the Company (FY24)	Revenue from Operations (INR in Mn)	AUM (INR in Bn)	CMP	P/E (x)	P/B (x)	Basic EPS (INR)	Capital Adequacy (%)	Return on Assets (%)	Return on Net worth (%)	Gross NPA (%)	Net Asset Value per equity share (INR)
Northern Arc Capital Limited*	18,901	117	263	13.4	1.5	19.7	18.3	2.97	13.3	0.45	174.5
Five-Star Business Finance Limited	21,828	96.4	743	25.9	4.2	28.6	50.5	8.37	16.1	1.38	177.7
SBFC Finance Limited	10,186	68.2	84	35.8	3.3	2.4	40.5	3.68	8.5	2.43	25.9
CreditAccess Grameen Limited	51,667	267.1	1,254	13.8	0.7	90.9	23.1	5.88	5.0	1.18	1,809.9
Fusion Micro Finance Limited	23,167	114.8	308	6.1	1.1	50.3	27.5	4.81	17.7	2.89	281.9
Bajaj Finance Limited	549,695	2,448.3	7,428	31.4	6.0	236.9	22.5	4.44	18.8	1.05	1,239.0
Cholamandalam Investment and Finance Company Limited	191,396	1,455.7	1,576	38.3	6.8	41.2	18.6	2.53	17.5	3.54	233.3
Poonawalla Fincorp Limited	31,090	250.0	397	18.3	3.8	21.6	33.8	10.02	20.6	1.16	105.4
MAS Financial Services Limited	12,792	101.3	280	18.3	2.6	15.3	24.1	2.95	14.1	2.25	108.7

Source: IPO Prospectus, KRChoksey Research; Note: *calculation of EPS, NAV and P/B based on post-IPO adjustments

Key Highlights:

- NACL is among India's diversified NBFCs in terms of AUM as of March 31, 2024, with a diversified business model across offerings, sectors, products, geographies, and borrower segments.
- Among the peer group considered for peer analysis, MSME players, on average, grew at a CAGR of 41.18% between FY22 and FY24 as compared to 36.86% of MFI players and 31.39% of diversified players among the peer group during the same period in terms of AUM. NACL has grown with a CAGR of 28.35% between FY22 and FY24 in terms of AUM.
- As of FY24, NACL has the lowest GNPA at 0.45% followed by Bajaj Finance (1.05%) among peers. As of FY24, Northern Arc has the lowest NNPA among peers at 0.08%, followed by Credit Access Grameen (0.35%).
- In terms of credit cost, Poonawalla Fincorp has the lowest credit cost as of FY24 among the peers for which data is available at 0.35%, followed by Five Star Business (0.55%). NACL has a credit cost of 0.47% as of fiscal 2023 and a credit cost of 1.18% as of FY24. Further, NACL has one of the lowest industry-wide credit costs amongst diversified NBFCs in India as of March 31, 2024.

Northern Arc Capital Ltd.

Financials:

Income Statement (INR Mn)	FY22	FY23	FY24	Cash Flow (In INR Mn)	FY22	FY23	FY24
Interest Income	7,808	11,484	17,121	Net Cash Flow from Operating Activities	-13,255	-12,957	-21,344
Finance Cost	4,107	5,574	7,264	Net Cash Flow from Investing Activities	-3,855	-1,195	360
Net Interest Income (NII)	3,702	5,909	9,857	Net Cash Flow from Financing Activities	20,281	9,280	20,455
Other Income	1,357	1,628	1,939	Net Increase/(Decrease) in Cash	3,171	-4,872	-529
Total Operating Income	5,059	7,538	11,796	Cash & Cash Equivalents at the Beginning	3,981	7,152	2,323
Operating expenses	2,210	3,914	6,360	Additions on acquisition of specified assets and liabilities	0	43	0
Pre-Provision Operating Profit (PPOP)	2,849	3,623	5,436	Cash & Cash Equivalents at the End	3,981	7,195	2,323
Provisions	365	392	1,224				
Profit before tax	2,484	3,231	4,212				
Share of loss from associates	0	19	10				
Tax expense	665	790	1,025				
Profit after Tax before minority interest	1,819	2,422	3,177				
Non-controlling interest	94	122	94				
Net Profit	1,725	2,300	3,083				
Basic EPS (INR)	19.5	25.9	34.6				
Diluted EPS (INR)	13.1	17.4	23.4				
Adjusted EPS (INR)	11.3	15.0	19.7				

Source: IPO Prospectus, KRChoksey Research.

Balance Sheet (INR Mn)	FY22	FY23	FY24
Financial Assets			
Cash & Cash equivalents	7,152	2,323	1,794
Bank Balances other than Cash & Cash Equivalent	873	1,903	2,283
Receivables	192	286	253
Loans	52,088	68,886	92,096
Investments	17,658	17,627	17,807
Other Financial Assets	712	1,116	1,387
Total Financial Assets	78,674	92,142	115,621
Non-Financial Assets			
Current tax Assets (Net)	421	291	240
Deferred Tax Assets (Net)	137	352	348
Property, Plant & Equipment	20	38	67
Intangible assets under development	3	10	23
Other intangible assets	94	134	118
Other non-financial assets	393	749	660
Total Non-Financial Assets	1,067	1,574	1,455
Total Assets	79,741	93,716	117,077
Liabilities			
Financial Liabilities			
Payables	558	1,096	1,285
Debt Securities	13,436	12,243	14,137
Borrowings (other than debt securities)	45,994	57,703	76,340
Derivative financial instruments	64.38	22.76	29.87
Subordinated Liabilities	399	400	0
Other Financial Liabilities	669	1,102	1,551
Total Financial Liabilities	61,122	72,566	93,343
Non-Financial Liabilities			
Current tax Liabilities (net)	0	0	46
Provisions	225	334	321
Other non-financial liabilities	74	138	163
Total Non-financial Liabilities	298	472	530
Equity			
Equity Share Capital	889	890	894
Instruments entirely equity in nature	826	826	826
Other Equity	15,675	17,837	21,424
Total Shareholders' Fund	17,391	19,554	23,144
Non-controlling Interest	930	1,123	60
Total Equity & Liabilities	79,741	93,716	117,077

Source: IPO Prospectus, KRChoksey Research.

Northern Arc Capital Ltd.

ANALYST CERTIFICATION:

I, **Dipak Saha** (MBA, Finance), Research Analyst, author and the name subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect my views about the subject issuer(s) or securities. I also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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