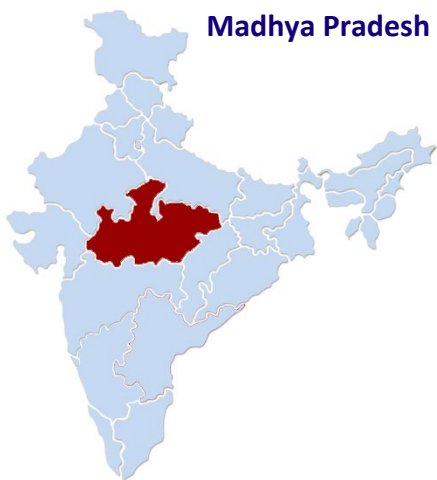


Madhya Pradesh



Insights from Ground Zero: Indore and Bhopal

- This is the second installment of the series that we started last year. In this series, we present our observations and findings from our branch/site visits, interactions with field staff or branch/area/regional/zonal managers and meetings with channel partners. Our endeavor remain the same i.e to pen down these observations with the utmost neutrality rather than coloring them with any investment recommendation bias.
- As is the case with such field visits, we would add the caveat that not everything we gather at the branch level or during our regional channel checks can be extrapolated at the national level, because of the subtle nuances across the length and breadth of our country.
- **This travelogue covers our visits to Indore and Bhopal**, the biggest markets in Madhya Pradesh, in the last week of Sep'23. Within a span of two days, we attended center meetings, visited branches and met branch/area/regional/zonal heads of the following companies:
 - **Vehicle Finance:** Mahindra Finance
 - **Gold Finance:** Manappuram Finance and IIFL Gold Loans
 - **Housing Finance:** Aavas, PNB Housing and IIFL Home Loan
 - **Microfinance:** CreditAccess Grameen and Fusion Microfinance
- In this report, we first summarize our key takeaways from the respective sectors, viz., vehicle financing, gold finance, housing finance and microfinance, and then delve deeper into our observations.

Vehicle Finance: Weak demand in entry-level PVs; minor impact of monsoons/floods on collections

- Demand for vehicles improved in Sep'23 compared to Aug'23, which was impacted by a weak monsoon. The supply of vehicles has largely normalized and there are no supply chain-related issues.
- There were slightly higher delinquencies and lower collections particularly in Jul'23-Aug'23 in certain parts of the country because of floods. However, there are no early warning signals. The asset quality should remain stable (with a minor improvement bias) in 2QFY24 and should improve further in 2HFY24.
- Even though a player like Mahindra Finance is aggressive in select M&M vehicle segments and select models of other OEMs, the endeavor is to maintain stable IRRs without any further compression in the yields.

List of companies

CreditAccess Grameen

Fusion Microfinance

Aavas Financiers

Mahindra & Mahindra Finance

PNB Housing Finance

Manappuram Finance

IIFL Finance

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Gold Finance: Muted loan and tonnage growth for mono-line gold financiers; competitive intensity higher in Sep'23 vs. prior months

2Q is typically the weakest quarter of the fiscal year. After strong growth in 4QFY23 and 1QFY24, we saw that the gold loan growth was muted in 2QFY24. For the six gold branches we visited, we have the following observations:

- Gold loan growth was muted in Jul'23, Aug'23 and Sep'23. There were large number of requests from customers for gold releases (mainly to use gold ornaments for personal use during the festive period from Ganesh Chaturthi to Deepawali). Tonnage growth should also remain modest because of high gold ornament release requests from customers.
- Competitive intensity was higher in Sep'23 than in Jul'23 and Aug'23. Competitive intensity was higher from banks and NBFCs like IIFL Finance and Bajaj Finance.
- Players like Rupeek and Muthoot Mercantile are offering up to ~80-85% LTV on gold loans by bundling a micro personal loan (micro-PL) along with a gold loan. Even Chola Finance has partnered with Rupeek to offer a bundled personal loan along with gold loans offered by Rupeek (and Federal Bank as the bank partner). Muthoot Finance is also offering a bundled gold loan and a micro-PL product only to its customers that have a healthy track record.
- In the last week of Sep'23, most of the gold lenders tried to spur their gold loan growth by offering attractive interest rates even at the ticket sizes between INR100k and INR500k. If these low interest rates (12% p.a. or 1% p.m.) schemes were to persist for lower ticket gold loans, it could even lead to minor pressure on yields.

Housing Finance: Slowdown in the lower-ticket housing loans, but no impact of high interest rates on asset quality

- Multiple interactions with zonal/regional/area managers and senior management teams of various HFCs suggest that there is a slowdown in mortgages, particularly in ticket sizes between INR1.5m and INR3.0m. On the contrary, business volumes suggest that there is no slowdown in the INR1.0-1.5m ticket segment.
- A large part of this slowdown is seen in the urban affordable and apartment-led affordable housing loans. Self-construction housing loans still remain buoyant.
- Most HFCs have transmitted higher interest rates to customers, but this has not led to any increase in delinquencies while collections remain robust. Collection efficiencies were largely stable in 2QFY24 (vs. 1QFY24) and HFCs are now able to leverage SARFAESI to achieve resolutions in NPA accounts.

Microfinance: Still going good; no impact of upcoming elections as yet

- Center meeting attendance is now lower than the pre-Covid level. Rural areas have better attendance than urban/semi-urban centers. New customer-acquisition led growth continues for microfinance firms.
- We do not see any impact of the upcoming state elections on collections or asset quality as yet. We do not expect any broad-based loan waivers (at the state level) in states headed for elections.
- While there would be flows across asset quality buckets, we expect asset quality to remain robust and credit costs to remain benign in the foreseeable future.

CreditAccess Grameen



Visited Mhow Gaon and branch around ~50km on the outskirts of Indore

- We attended two kendra (center) meetings. Women borrowers were predominantly rural customers who were working as laborers in fields, construction and masonry. Most of them had taken loans to buy cattle (cow, buffalo or goats) and were either engaged in milk supply to the dairy or rearing of goats.
- Customers who were part of the group were either in their first or second cycles since CREDAG started operations in this district around two years ago in mid-2021. Loans of INR30k-40k were given to the first cycle customers. Loans up to INR30k were for tenors of 1 year and all loans above INR30k were for tenors of 2 years.
- Each kendra typically conducts a mini-meeting on the day prior to the EMI date and the center leader collects EMIs from the different members of the group. On the day of the group meeting, the kendra officer (loan officer/relationship officer) conducts the center meeting, collects installments from customers and appraises them of the various Do's and Don'ts.
- Installment frequency was weekly; Customers were divided over whether a weekly or monthly EMI frequency would be better. Few suggested that a monthly EMI would have been better since weekly center meetings were a big overhead, while others suggested that smaller EMIs under the weekly repayment model were better for them.
- Key competitors in the region were IDFC First, Ujjivan and Belstar. On average we found that ~40% of the members in the group had only one loan and the remaining had two/three loans from other key players in the region.
- Customers shared that IDFC First and Belstar did not conduct center meetings (like CREDAG did) but instead just sent the personnel to collect the installments from customers.
- Customers understood that defaulting on their loans would impact their credit bureau score and this would make them ineligible for availing loans in the future. We did not see 100% attendance in any of the center meetings; One/two members in the group were absent from the center meeting for some reason or another.

Branch visit and meeting with Zonal Manager

- Loan demand remained strong, but the competitive landscape was not benign; CREDAG was charging 21.5-22% interest rates in the region.
- Attrition existed predominantly at the field officer (FO) level, but it was stable among the employees above the area manager level. There is no lateral hiring at the FO level and only freshers are recruited and given classroom and field training.
- No visible signs of any asset quality stress in the portfolio; there were minor niggles when the rains were weak or when there is flooding in some places, but nothing alarming on the collections front.
- Elections are coming up in Nov/Dec'23 but we see no impact of elections on the collections just yet; suggested that there should not be any major impact from the upcoming elections on asset quality.
- CREDAG is further strengthening the risk management function by increasing the frequency of audits of the branches.

Fusion Microfinance



Semi-urban set-up

- The proportion of customers unique to Fusion was lower than that of CREDAG . In the center meetings, customers also had MFI loans from the likes of Jana Lakshmi, IndusInd and Yes Bank.
- Attendance was lower in the urban centers vs. rural centers.
- Most customers had a view on whether the monthly or weekly EMIs were better. Urban/Semi-urban customers seemed to suggest that the monthly installments were better even though the EMI amount was higher (vs. weekly EMIs).
- Even though state elections are due in Dec'23, there was no individual or political party trying to influence customers into believing that their loans would be waived off. Customers were also educated that any defaults on their loan will spoil their credit bureau records.
- In the first cycle, Fusion was providing loans of ~INR40k; many centers had customers with high vintages and who were in their 3rd or 4th cycles with Fusion and had higher loan amounts.
- Fusion is looking to bring down the number of customers per field officer down to 600 by adding more field officers in branches.
- Employees are incentivized for customer additions and not for disbursements.
- Mandatory for customers to visit the branches for loan disbursement, irrespective of their vintage and/or loan cycles.
- No impact of floods in MP, while Eastern Bihar and Eastern UP could have had some impact because of the floods.
- Fusion provides a maximum ticket size of INR80k to customers; the cumulative loan amount across all lenders should not exceed INR250k.

Aavas Financiers



Branch visit in Bhopal and meeting with Zonal Sales and Credit Managers

- Aavas has three broader verticals: Affordable (EWS), LIG/MIG and Retail. Both the affordable and LIG/MIG teams work very closely with the state/local municipal and housing boards.
- On the demand front, Aavas is not witnessing any signs of a slowdown. After the CLSS subsidy has been withdrawn, supply has been little muted in the affordable sector but the self-construction segment continues to do very well.
- MP is an agriculture belt and is a good affordable housing region in India. Recently, there have been new entrants in MP like Ummeed Housing Finance, JM Housing Finance, Adani Housing and Fed Financial Services.
- Teething issues from the SFDC implementation (from 1st Apr'23 onward, pan-India) have now largely been addressed. There are very minor glitches for which the team keeps giving input to the tech implementation team. It expects the business momentum to pick up significantly in 2HFY24.
- TAT improved significantly after the implementation of the SFDC platform. TAT has now declined to 5-6 days from 10-11 days earlier. Aavas expects TAT to come down by another one day after disbursement activity is also integrated into the new SFDC platform.

- While a large part of the sourcing and underwriting (technical/legal) is done in-house, it has started leveraging vendors when the business volumes are high (like toward month-end or quarter-end).
- In addition to in-house sourcing (DST) and the Mitra Channel, it is also trying to develop the lead providers (LP) channel.
- Among peers, both Bandhan Bank and Aadhar Housing come across as the most aggressive. However, Aavas's deeper distribution (relative to its peers) serves it well.
- Asset quality has been holding up well. It has not seen any increase in delinquencies after higher interest rates were transmitted to borrowers.

Mahindra Finance

Mahindra FINANCE

Branch visit in Indore and meeting with divisional heads

- Demand was little muted when the monsoons were weak in Aug'23, but it recovered in Sep'23 due to good rainfall. We have seen good improvement in demand for trade advances from dealers as well. The festive season should be good and along expected lines.
- Car loan disbursements grew ~35% YTD (ex-M&M vehicles) and the number of dealers almost doubled under the mass scheme (lower IRR scheme). Delinquencies are almost ~50% lower since customer cash flows have improved. MMFS has improved internal processes. Mahindra One App (rolled out in the last 6-8 months) provides CIBIL bureau check almost instantly, which makes the decision-making process faster and better. The dedupe process is more robust compared to earlier days.
- In products like XUV, Thar and Scorpio-N, volumes are limited and supply chain constraints are still there, leading to a long waiting period for these vehicles.
- Sectoral tailwinds have helped MMFS, but the process/checks have also been significantly improved.
- Collections are now being monitored at the bucket levels, with separate collection teams for the four different buckets.
- Until now, disbursements were decentralized; Delivery orders (DO) were earlier issued at the branch level and they had to look at delivery orders across all verticals. Maharashtra is already doing pilots under the CPC model and MMFS expects that within the next 2-3 months, the CPC will be rolled out across India. CPC will be deployed across all Wheels businesses and will significantly improve the TAT and the sanction/disbursement momentum.
- Earlier both M&M and MMFS used to hold discussions separately (and in parallel) with M&M dealers. Now the synergies between M&M, MMFS and the dealers have significantly improved.
- Even though the company has been catering to Prime customers (better credit quality customers), the endeavor has been to maintain average IRRs at the branch level and the divisional levels. It aims to maintain 40% market share (in MP) in the M&M personal segment and ~35% at the pan-India level. MMFS is competing effectively in products like XUV family and Scorpio-N but makes up for it with higher pricing in products like Mahindra Scorpio Classic and Bolero.

PNB Housing Finance



Branch visit and meeting with regional sales head

- Demand is holding up well and the company has not seen any signs of a slowdown in mortgages in the MP region.
- PNBHF earlier used to do both high and low ticket-size mortgages - both Home loans as well as LAP. However, for the last one year, its retail lending segment has been focusing on properties where the ticket size is less than INR10m (up to INR50m earlier).
- PNBHF operates under a hub-and-spoke model. Indore, Bhopal, Jabalpur and Raipur are hubs in MP. The hub will require less manpower as online/digital processing gains prominence. Each hub has a credit manager who caters to the spoke branches.
- Few large private banks have reduced their focus on channel partners and have increased the proportion of direct sourcing. Earlier banks used to pay out incentives/commissions to channel partners without any claw-back provisions. Now few banks have introduced claw-back provisions that if the customer takes a balance transfer within one/two years, a proportion of the commissions paid will be clawed back.
- DSA commissions range around 80-85bp in home loans and 80-135bp in LAP.
- Over the last one year, the focus on technology has increased for bringing more efficiency to the sourcing function. Digital technology is effectively being leveraged for sourcing.
- PNBHF is again becoming competitive in the mortgages space (probably because of its expectations that its cost of borrowings will trend down over a course of time). It is competitive in home loans (relative to larger HFCs and Banks) within the prime segment (not to be misinterpreted as super-prime segment). In this segment, PNBHF's home loan interest rates are 10-25bp higher than banks'.
- Roshni business, the affordable housing finance, has been started as a completely separate vertical with its own set of employees, channel partners and branches.
- Asset quality has held up well and it has not seen any increase in delinquencies even after transmitting higher interest rates to customers. SARFAESI and DRT Act have played a big role in structural improvement in asset quality within mortgages. Earlier, a hard recovery was prominent but is no longer the case since the customer understands that the property goes for liquidation/auction, the distressed sale will fetch a lower amount and is not favorable for the customer.

Manappuram Finance



Branch visit in Indore and Bhopal

- Demand for gold loans was sequentially weaker and most branches we visited suggested that they saw marginal or flat growth in gold loans during the quarter. Even at the regional and state level, we saw a similar trend in gold loans.
- The release of gold jewelry was also higher particularly in Sep'23 because of many festivities. This could also result in a lower gold tonnage vs. prior quarter.
- Unlike Muthoot, which has introduced a bundled gold loan product (Gold loan + Micro PL) for customers with a good track record, MGFL is not giving any bundled gold loan products to customers.
- There are multiple schemes for gold loan takeovers from PSU Banks, NBFCs and local gold loan financial institutions.
- Competitive intensity higher vs. the last two quarters. Competition not just from banks but also from NBFCs like IIFL Finance, Bajaj Finance and Capri Gold Loans.
- Lower interest rate schemes were launched in the last two weeks of Sep'23 to spur gold loan demand.
- MGFL provides online function (through its app - Online Gold loan - OGL) for customers to re-pledge their gold jewelry and avail a lower interest rate if they accept a lower LTV on their gold loan (by making part-payment of principal).
- MGFL has implemented security measures such that none of the branches now require any lock and key and presence of a security guard at the entrance. This would have brought down the security costs of the branch.

IIFL Finance



Gold Loan: Branch visit in Bhopal

- Gold loan growth continued to remain strong even in a seasonally weak quarter.
- Co-lending forms a sizeable proportion of gold loans, which allows the company to offer attractive interest rates on gold loans.
- It has launched several initiatives and frequent schemes to win back old customers and to add new gold loan customers.
- Gold loan branch employees visit the field for marketing activities and identifying gold loan customers. They originate gold loans by visiting customers and getting them to the branch for gold loans.
- High security is maintained at each branch with use of lock and key. Whenever a customer visits the branch, the main door has to be opened by employees from inside the branch.
- Bajaj Finance (BAF) and Fed Financial (FedFina) have been aggressively competing for gold loans in Bhopal. Like IIFL Finance, even BAF and FedFina offer 2-year gold loan products. BAF has been aggressively adding standalone gold loan branches (SGB).
- Following scheme was among the lowest interest rate schemes: Ticket size of >INR500k; interest rate of 1.0% p.m.; full LTV was offered along with quarterly interest repayment.
- In the last week of Sep'23, Muthoot Finance launched a 0.9% p.m. (monthly interest payment) scheme for all ticket sizes above INR100k.
- Muthoot Mercantile is offering a much more attractive per-gram gold loan rate compared to other gold loan lenders.

Home Loan: Branch Visit in Indore

- The first half of the fiscal year is usually leaner than the second half. Business growth is strong as the company is clocking the same volumes it did in 4QFY23.
- Banks are not able to do justice to the affordable housing segment and need partners that can efficiently deliver services in deeper Tier 2/3 locations. Banks have a brand pull, while lenders like IIFL need to put in efforts and compensate for slightly higher interest rates with their better service, which includes a complete digital delivery at the customer's doorstep.
- Builders do not charge commission and even if they do, they are much lower than other channel partners. The ultimate interest of a builder is to get paid the money at the earliest.
- IIFL is one of those few HFCs that can genuinely disburse a loan within 24 hours.
- Housing demand is relatively weaker in ticket sizes of up to INR3m. Many customers preponed their housing purchases over the last two years. This is resulting in a temporary lull in demand.
- Supply is also a constraint in some of the apartment-led affordable housing belts. However, self-construction continues to do very well.
- Corporate DSAs are paid out commissions of ~1% for Home Loans and ~1.5% for LAP.
- IIFL has a minor share of loans originated through the DSA channel. IIFL focuses on loan originations through Approved Project Financing (APF) and its own DST channel. Insurance penetration in the DST channel is 4-5% vs. 1% in the DSA channel. The DSA channel is vulnerable to DSAs' partnerships with another insurance agency, higher BT-OUTS and constant churn in customers.
- A centralized credit team provides the soft sanction or the financial sanction. The final sanction/credit is done by the respective local hub.
- IIFL Finance has also steadily built a loan book in the micro LAP segment. Its Shakti micro-LAP product has a ticket size in the range of INR200k to INR1m and it charges a flat ~24% interest rate. IIFL has built a Micro-LAP book of ~INR10b. This product has LTV in the range of 40-60% and a loan tenor of seven years.

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