NORTHERN ARC CAPITAL LIMITED

September 13, 2024

SMC Ranking

★★☆☆☆ (2/5)

Issue Highlights

Industry	NBFC
Offer for sale (Shares)	1,05,32,320
Fresh Issue (Shares)	1,90,11,407
Net Offer to the Public	2,95,43,727
Issue Size (Rs. Cr.)	735-777
Price Band (Rs.)	249-263
Employee Discount	Rs.24 per share
Offer Date	16-Sep-24
Close Date	19-Sep-24
Face Value	10
Lot Size	57

Issue Composition

	In shares
Total Issue for Sale	3,20,31,250
QIB	1,47,71,864
NIB	44,31,559
Retail	1,03,40,304

Shareholding Pattern (%)

Particulars	Pre-issue	Post -issue
Promoters & promoters group	0.00%	0.00%
QIB	96.49%	87.75%
NIB	3.51%	5.84%
Retail	0.00%	6.41%
Total	**100.00%**	**100.00%**

*calculated on the upper price band

Objects of the Issue

The company proposes to utilize the Net Proceeds to meet future capital requirements toward onward lending.

Book Running Lead Manager

- ICICI Securities Limited
- Axis Capital Limited
- Citigroup Global Markets India Private Limited

Name of the registrar

- KFin Technologies Limited

About the company

Northern Arc Capital Limited 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 company has facilitated over Rs. 1.73 trillion worth of financing, reaching out to over 101.82 million people across India. 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 been active in MSME finance for over 14 years, MFI finance for 15 years and consumer finance for nine years. The company serves the retail lending market through a multi-channel approach that includes Lending, Placements and Fund Management. The company also has an end-to-end integrated technology product suite customized to multiple sectors. This includes an in-house technology stack consisting (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 originator partners in the loan underwriting process; and (iv) AltiFi, an alternative retail debt investment platform.

Strength

Expansive Market Potential with Deep Sector Expertise: Northern Arc Capital Limited has established itself as a leader in providing credit across various sectors, leveraging its diversified business model and proprietary technology suite tailored to multiple industries. Over the last 15 years, the company has developed strong expertise in sectors such as MSME, MFI, consumer finance, vehicle finance, affordable housing finance, and agriculture finance. Northern Arc Capital has been active in the MSME, MFI, and consumer finance sectors for over 14, 15, and 9 years, respectively. Recently, the company expanded its retail MSME services by launching Loan Against Property (LAP) financing in Fiscal 2022 and supply chain finance in Fiscal 2023. As of March 31, 2024, its LAP financing operations, through 50 branches, offer secured business loans to MSMEs, while its technology-driven supply chain finance solutions provide funding to participants across the supply chain network. Additionally, Northern Arc incorporated its rural finance subsidiary, Pragati, in Fiscal 2021, which serves rural and semi-urban areas, offering small-ticket loans through a digital platform. The company also provides a broad portfolio of products in the consumer finance sector, including consumer durable loans, personal loans, salary advance loans, and buy-now-pay-later financing through both online and offline channels in collaboration with retail lending partners.

Strong Ecosystem and Technological Network Effects: Over the past 15 years, Northern Arc Capital Limited has built a robust ecosystem in the Indian retail credit market, facilitating financing of over Rs.1.73 trillion since 2009, impacting over 101.82 million lives as of March 31, 2024. The company's network consists of 328 Originator Partners, 50 Retail Lending Partners, and 1,158 Investor Partners, supported by multi-channel offerings such as lending, placements, and fund management. With a proprietary technology platform and a data repository of over 35.17 million data points, the company continues to expand its debt-raising and investment opportunities. This ecosystem provides Northern Arc access to large pools of liquidity, allowing the company to serve a wide range of investors and generate annuity income from both fee and interest revenues.

Innovative Proprietary Technology Transforming Debt Markets: Northern Arc Capital is a technology-driven financial services platform, utilizing in-house solutions to foster business scalability and growth.

Its flagship technology, **Nimbus,** is an integrated platform facilitating the end-to-end processing of debt transactions. Nimbus streamlines the flow of credit from Originator Partners through the company's balance sheet or Investor Partners, handling everything from loan application to transaction execution. The platform enhances scale, precision, transparency, and efficiency in processing debt transactions and enables seamless information exchange between partners. Nimbus also covers internal functions such as partner onboarding, credit evaluation, and post-transaction compliance. As of Fiscal 2024, Nimbus facilitated credit of Rs.997.16 billion with 147 Originator Partners and 72 Investor Partners.

The **nPOS** platform, another key innovation, is a cloud-based API-enabled system that automates and speeds up the loan process for partnership lending, allowing data exchange and loan processing without manual intervention. Its scalable design integrates external partners such as credit bureaus, offering a seamless experience for financial institutions and Originator Partners. In Fiscal 2024, the platform handled transactions worth Rs.5989.06 crore and was recognized as the 'Best Lending Fintech Platform.'

AltiFi, another product, democratizes access to debt capital markets for retail investors, HNIs, and small corporates. It offers fixed income instruments previously accessible only to institutional investors, diversifying portfolios and reducing exposure to market volatility. As of March 31, 2024, AltiFi had over 30,518 registered users and facilitated Rs.4,163.29 million in investments.

Comprehensive Risk Management: Risk management is central to Northern Arc Capital's operations, spanning all sectors and borrower categories. Over time, the company has developed a tailored risk management system, using its expertise and data to create proprietary risk models customized to its offerings and markets. These systems enable Northern Arc to maintain a diversified portfolio and proactively manage risks. Most of the company's credit risk management processes are enhanced through deep analytics and early warning systems on its Nimbus platform, helping minimize risks. As a result, the company reported a Gross Non-Performing Assets (GNPA) ratio of 0.45% and a Net Non-Performing Assets (NNPA) ratio of 0.08% as of Fiscal 2024, one of the lowest in the industry.

Diversified Funding Sources and Liquidity Management: Northern Arc maintains a diversified funding profile through relationships with a broad base of lenders, including banks, offshore financial institutions, and NBFCs, as well as its investor network. Over the past 11 years, the company has conducted 12 rounds of equity fundraising, benefiting from investments by leading equity investors, including impact-focused funds and global banks. Northern Arc also maintains a positive asset-liability management (ALM) position, ensuring no cumulative negative mismatches within one year, and complies with liquidity coverage ratio (LCR) norms by investing in low-risk, short-term instruments.

ESG Integration and Sustainable Impact: Northern Arc integrates ESG practices into its business model, following the LeapFrog group's 'Responsible Investment Code,' which emphasizes delivering both financial and social impact. The company has an ESG officer and team responsible for overseeing practices, ensuring compliance with responsible financing frameworks and environmental, social, and governance parameters. Northern Arc also encourages its Originator Partners to adopt sustainability alignment tools based on UN Sustainable Development Goals (UNSDGs). As of December 31, 2023, 43.96% of borrowers were women, reflecting the company's commitment to fostering inclusion and sustainability

Strategy

Enhance the ecosystem by strengthening partnerships and scaling technology: The company aims to expand its presence to better serve underserved households and businesses in key sectors across India. This will be achieved by (i) increasing the number of Originator Partners and Retail Lending Partners to finance debt capital requirements and expand its reach to Direct-to-Customer Borrowers, and (ii) leveraging its in-house technology and data-driven platforms. By doing so, the company seeks to broaden its investor base, reaching new classes of investors domestically and overseas, such as NBFCs, AIFs, private wealth investors, distributors, and institutional investors, insurance companies, pension funds and corporate treasuries. As current Investor Partners deepen their understanding of the company's focused sectors, they are expected to diversify their portfolios, leading to increased financing volumes and wider impact. By collaborating with Originator Partners and Investor Partners and continuously innovating, the company facilitates seamless credit transfer to end customers.

Expand into adjacent sectors and enhance ESG risk management: The company plans to explore new opportunities in adjacent sectors like climate lending and gold loans. It aims to collaborate with Originator Partners to participate in climate and sustainability projects, particularly in MSMEs. The climate financing industry in India is experiencing significant growth, especially in renewable energy, and the company seeks to work with environmentally conscious businesses to finance solutions like electric mobility, solar energy, waste recycling, and sustainable water management. As of March 2024, the two leading power financing companies in India possessed gross loan assets of Rs.992 billion towards renewable energy sector, underscoring not just their current standing but also signalling the vast potential for expansion in other climate financing aspects. This robust foundation and continued governmental backing position the sector for further sustainable development and environmental impact. Additionally, it will engage with lenders who finance these climate-friendly

products for end customers, contributing to sustainability and environmental impact.

Expand the company's Fund Management channel: In the company's Fund Management channel, Northern Arc Capital Limited is focused on capitalizing on the company's innovative products, track record of returns and established investor base to further deepen the company's offerings and scale the company's business. It aims to expand the company's Fund Management business through:

- **Product innovation:** The Company intends to launch thematic funds targeting climate, agriculture, financial services and gender. Further, Northern Arc Capital Limited is also focused on expanding the focus of the company's funds. For instance, the company's Emerging Corporate Bond fund, launched in Fiscal 2023, was focused on new age businesses and SME. It intends to launch additional funds with a similar focus as well as add structured investments based on collateral such as real estate and equity. For the company's PMS offering, it aims to launch interval funds and custom corporate focused yield/ tenor funds that are targeted towards retail and corporate investors.

- **Geographical expansion:** In addition to the company's current Mauritius fund, Northern Arc Capital Limited and intend to continue to grow the company's 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. In addition, it will look to establish offshore vehicles in favorable locations in the future.

- **Expand investor categories:** It aims to increase the company's investor base by targeting new investors, particularly in Asia as well as deepen the company's relationships with the company's existing European and United States investor base. In India, the company's PMS funds have onboarded both corporates and smaller ticket investors through independent financial advisors and the company's new fund launches are aimed towards broadening this investor category. Further, the company's specific higher yield products are aimed for international funds-of-funds, sovereign wealth funds, foundations, endowments and pension funds. Moreover, Northern Arc Capital Limited and intend to continue to focus on specific funds that target HNIs, family offices and corporates, which has helped in expanding the company's reach in these investor categories. In addition, we intend to continue to leverage and grow the company's PMS offerings in order to provide it access to a wider investor base comprising private wealth investors and HNIs.

Scaling Direct-to-Customer Lending for risk-adjusted returns: The company intends to expand its Direct-to-Customer Lending channel to tap into India's growing retail credit market. This involves increasing its presence in existing states, expanding into new geographies, and introducing new product offerings for borrowers. By leveraging its 'phygital' presence, combining physical branches with digital platforms, the company will continue to scale its retail lending operations. Strategic collaborations with Retail Lending Partners and a strong rural finance network will enable the company to provide a wider range of credit solutions, enhancing risk-adjusted returns.

Focus on credit quality for efficient credit cost management: The company adheres to a 'credit first' principle, ensuring superior credit quality and lower credit costs by integrating data and technology into its operations. It monitors customers in real-time

and uses predictive, data-driven decision-making to manage credit risk efficiently. Key practices include identifying early warnings, monitoring borrowers' repayment behavior, and analyzing geographical risks. By investing in risk monitoring and machine learning, the company seeks to develop a comprehensive credit cost management framework and strengthen its credibility with Investor Partners in its Placements and Fund Management channels.

Diversifying funding sources and optimizing borrowing costs: The company is committed to diversifying its borrowing profile and maintaining a positive asset-liability management (ALM) position. By improving its credit rating and optimizing borrowing costs, the company can competitively price its loan products and increase its market share. It aims to diversify its lender base, secure long-term funding, and engage with international investors, including multilateral institutions. Additionally, it will continue to grow its Direct-to-Customer Lending business and explore sell-down opportunities through direct assignments to strengthen its financial position.

Inorganic growth opportunities: In addition to organic growth, the company will pursue strategic acquisitions, alliances, partnerships, and joint ventures to enhance its position in the financial ecosystem. These initiatives will enable the company to tap into new markets, grow its revenues, and expand its footprint through inorganic growth.

Risk factor

- The company operates a diversified business model that exposes it to various risks and an inability to manage such risks may have an adverse effect on its business, results of operations, cash flows and financial condition.
- A significant portion of its investments are in credit facilities and debt instruments that are unsecured, and/or subordinated to other creditors.
- Its inability in the future to comply with or any delay in compliance with the strict regulatory requirements with respect to its listed non-convertible debentures may have an adverse effect on its business, results of operations, cash flows and financial condition.
- The company operates in a highly competitive industry and its inability to compete effectively may adversely affect its business, reputation, results of operations, cash flows and financial condition.

Peer Comparison

Co_Name	Total Income	PAT	EPS	P/E	P/BV	BV	FV	Price	Mcap
Cholaman.Inv.&Fn	21122.57	3657.27	43.52	34.95	6.52	233.12	2.00	1521.05	127829.40
Bajaj Finance	58590.26	14926.26	241.14	30.48	5.96	1234.23	2.00	7350.25	454977.80
Poonawalla Fin	4258.76	1748.65	15.69	25.10	3.75	105.09	2.00	393.75	30604.02
Five-Star Bus.Fi	2380.91	903.78	30.90	23.97	4.17	177.66	1.00	740.80	21666.65
CreditAcc. Gram.	5514.50	1495.12	93.77	12.89	2.93	412.04	10.00	1208.45	19269.10
MAS FINANC SER	1363.45	265.85	14.65	19.06	2.22	125.80	10.00	279.25	5067.09
Fusion Microfin.	2566.32	349.21	34.70	8.96	1.10	283.03	10.00	310.75	3127.10
SBFC Finance	1087.77	269.05	2.50	33.56	3.25	25.85	10.00	83.89	9031.49
Northern Arc Capital Limited	1890.08	317.69	19.69	13.36	1.50	174.83	10.00	263.00	4242.86

***Peer companies financials are TTM based**
****Northern Arc Capital Limited is based on Fy24**

Valuation

Considering the P/E valuation, on the upper end of the price band of Rs.263, the stock is priced at pre issue P/E of 11.78x on FY24 EPS of Rs.22.32. Post issue, the stock is priced at a P/E of 13.36x on its EPS of Rs.19.69. Looking at the P/B ratio at Rs.263 pre issue, book value of Rs. 163.05 of P/Bvx 1.61x. Post issue, book value of Rs. 174.83 of P/Bvx 1.50x.

Considering the P/E valuation, on the lower end of the price band of Rs.249, the stock is priced at pre issue P/E of 11.15x on FY24 EPS of Rs.22.32. Post issue, the stock is priced at a P/E of 12.64x on its EPS of Rs.19.69. Looking at the P/B ratio at Rs.249 pre issue, book value of Rs. 163.05 of P/Bvx 1.53x. Post issue, book value of Rs. 174.83 of P/Bvx 1.42x.

Industry Overview

The Indian retail credit market is expected to further grow at a CAGR of 17-18% between Fiscals 2024 and 2026 to reach ₹100.9 trillion by Fiscal 2026. NBFCs loan outstanding for MSME, MFI, consumer finance, vehicle, affordable housing and agriculture loans are expected to grow at a CAGR of 13-15%, 23-25%, 17-20%, 12-14%, 14-16% and 9-10%, respectively, between Fiscals 2024-2026. Rural areas, which accounted for 47% of GDP, received only 9% 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.

Outlook

The company is a prominent non-banking financial company (NBFC) in India, boasting a diverse portfolio of lending services. With a strong focus on micro, small, and medium enterprises (MSMEs), microfinance (MFI), consumer finance, vehicle finance, affordable housing finance, and agriculture finance, the company has established a significant presence in these sectors. Its expertise in MSME finance spans over 14 years, while it has been involved in MFI and consumer finance for 15 and nine years, respectively. To support its operations, the company has developed a comprehensive technology platform. This includes Nimbus, a debt transaction platform, nPOS for co-lending and co-origination, Nu Score for loan underwriting, and AltiFi for retail debt investment. While its diversified business model offers opportunities, it also exposes the company to various risks. The ability to effectively manage these risks is crucial to maintaining its business, financial performance, and overall stability.

An Indicative timetable in respect of the Issue is set out below:

EVENT	INDICATIVE DATE (On or about)
IPO Open Date	Monday, September 16, 2024
IPO Close Date	Thursday, September 19, 2024
Basis of Allotment	Friday, September 20, 2024
Initiation of Refunds	Monday, September 23, 2024
Credit of Shares to Demat	Monday, September 23, 2024
Listing Date	Tuesday, September 24, 2024

Annexure

Consolidated Financials

Profit & Loss

Rs. in Cr.

Particulars	Period ended 31-Mar-24 (12 Months)	Period ended 31-Mar-23 (12 Months)	Period ended 31-Mar-22 (12 Months)
Revenue from operations	1890.08	1304.97	909.54
Total expenditure	741.50	418.61	247.91
Operating Profit	**1148.59**	**886.36**	**661.63**
OPM%	60.77	67.92	72.74
Other Income	15.95	6.23	7.01
Total Net Income	**1164.54**	**892.59**	**668.64**
Interest	726.39	557.45	410.67
PBDT	**438.15**	**335.14**	**257.97**
Depreciation	16.94	12.04	9.58
Profit before tax and share of profit or loss of associates	**421.21**	**323.10**	**248.39**
Share of profit / (loss) from associates	-0.97	-1.87	0.00
Restated Profit before tax	**420.24**	**321.23**	**248.39**
Tax	102.54	79.01	66.45
PAT	**317.69**	**242.21**	**181.94**

Balance sheet is on next page

Balance Sheet

Rs. in Cr.

Particulars	As on 31-Mar-24	As on 31-Mar-23	As on 31-Mar-22
Non-current assets			
Current tax assets (Net)	24.04	29.12	42.09
Deferred tax assets (net)	34.76	35.18	13.69
Property, plant and equipment	6.66	3.81	1.96
Intangible assets under development	**2.31**	**0.99**	**0.28**
Goodwill	23.48	24.07	1.75
Other intangible assets	11.79	13.37	9.43
Right of use asset	14.72	9.67	11.22
Investment in associates	3.89	27.27	0.00
Deferred tax assets (net)	23.88	13.91	26.33
Total non-current assets	**145.54**	**157.38**	**106.74**
Current asset			
Cash and cash equivalents	179.40	232.34	715.17
Bank balances other than cash and cash equivalents	**228.34**	**190.26**	**87.34**
Derivative financial instruments	54.82	61.05	1.52
Trade receivables	25.35	28.61	19.18
Loans	9209.59	6888.61	5208.76
Investments	1780.71	1762.73	1765.75
Other financial assets	83.92	50.59	69.65
Total current assets	**11562.12**	**9214.19**	**7867.38**
Total Assets	**11707.66**	**9371.57**	**7974.12**
Non-current liabilities			
Provisions	32.07	33.35	22.46
Lease liabilities	4.62	0.00	0.00
Other non-financial liabilities	15.56	13.64	6.67
Provisions	0.72	0.20	0.72
Total Non- Financial liabilities	**52.96**	**47.20**	**29.85**
Current liabilities			
Derivative financial instruments	2.99	2.28	6.44
Borrowings	7634.03	5770.30	4599.43
Debt securities	1413.73	1224.32	1343.60
Trades Payable - MSME	0.00	0.00	0.00
Trades Payable - MESE	128.48	109.61	55.82
subordinated liabilities	0.00	39.95	39.94
Other financial liabilities	155.06	110.19	66.94
Total Financial liabilities	**9334.28**	**7256.65**	**6112.16**
Total	**9387.25**	**7303.84**	**6142.00**
Net worth represented by:			
Equity Share Capital	89.39	89.03	88.91
Instrument entirely equity in nature	2142.35	1783.75	1567.52
Non controlling interest	6.03	112.30	93.03
Other equity	82.65	82.65	82.65
Net Worth	**2320.41**	**2067.73**	**1832.11**

RANKING METHODOLOGY

WEAK	★
NEUTRAL	★★
FAIR	★★★
GOOD	★★★★
EXCELLENT	★★★★★

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