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Northern Arc Capital

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INITIATING COVERAGE | **NORTHARC IN EQUITY** | **December 24, 2025**

Retail pivot mispriced

Market is undermining NACL's NIM/ROE improvement prospects likely due to legacy wholesale mix and recent high credit costs. But since pivoting to retail (D2C) in FY22, spread/ROE expanded 675bps/410bps. Continued transition to high-margin D2C will drive 15.7% ROE by FY28E. Long-vintage experience in finance placement and fund management will aid fee income, strengthening ability to absorb structurally higher credit cost while sustaining ROE>COE. Reducing overleveraging among bottom-of-pyramid would aid credit cost improvement (FY26-28E). Building vehicle/affordable home finance expertise through the intermediate retail route provides an option to add D2C growth levers. At <1x/<7x 1yr fwd BV/EPS, NACL offers structural transition to higher-ROE business + cyclical recovery in the near term with negligible downside. Risks: Slower asset quality recovery and slower D2C growth.

Competitive position: MEDIUM | Changes to this position: NEUTRAL

Lower spreads in intermediate retail lending weighed on ROE

Before embarking on retail-focused lending in 2018/19, NACL focused on intermediate retail lending (akin to wholesale) and financing placements. Given competitive rates in wholesale lending, AUM growth was limited to 14% CAGR (FY18-21). Average spread of 3.2% limited average ROE to 7.5% (FY19-21).

D2C pivot for scale. Optionality enhances long-term growth prospects

With retail pivot, D2C mix rose to 52% (FY25) vs 19% (FY21). Minuscule market share across retail categories, diversified state presence, fully integrated platform with distributors/digital platforms will aid 34% D2C AUM CAGR (FY26-28E), taking D2C mix to 64%. Vehicle/affordable home finance expertise through intermediate lending provides option to add growth levers (23% 10yr CAGR) vs nil portfolio currently. Expanding NBFC sector and emerging corporates to aid 12-15% placement volume/fund management CAGR (FY26-28E).

D2C-led NIM expansion + fee strengthen credit loss absorption buffer

With D2C yields 920bps higher than intermediate retail, we expect 70bps spread expansion by FY28E, supporting 10.7-10.9% NIMs. Fee income (15% CAGR FY26-28E) from placements/fund management to strengthen operating profit margin to 6.5-7%, increasing credit loss absorption buffer while sustaining 15%+ ROE. As asset quality headwinds subside, credit cost should reduce to 2.6% (FY27/28E).

Valuations undermine transition to a stronger business model

NACL is structurally transitioning from wholesale to retail-focused lender, a journey that entails structural ROE of 15% vs ~5% (FY21). While the current business model can aid 41% EPS CAGR (FY26-28E), longer-term growth longevity levers exist in scaling up vehicle/affordable home finance. 50-60% valuation discount to peers undermines improving prospects. Our fair value factors 20% AUM CAGR/15% average ROE (FY26-36E), implying 1.2x/10x FY27E BVPS/EPS.

Key financials

Particulars	FY24	FY25	FY26E	FY27E	FY28E
AUM (₹ bn)	117	136	160	200	245
AUM growth (%)	30	16	18	25	22
EPS (₹)	23.4	20.0	23.3	33.3	46.0
RoE (%)	14.5	10.5	10.4	13.2	15.7
P/B (x)	1.5	1.2	1.1	1.0	0.8

Source: Company, Ambit Capital research

NBFCs

Recommendation

Mcap (bn):	₹41/US$0.5
6M ADV (mn):	₹390/US$4.5
CMP:	₹254
TP (12-month):	₹326
Upside (%):	28

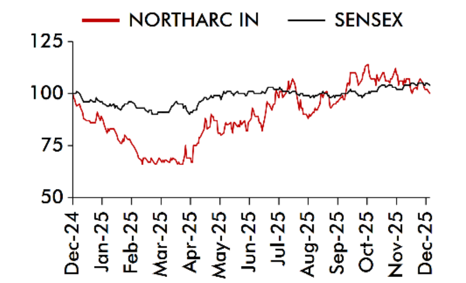
Flags

Accounting:	AMBER
Predictability:	AMBER
Earnings Momentum:	AMBER

Catalysts

- Increase in D2C mix to 60% to aid 42bps YoY spread expansion in FY27E.
- Subsiding systemic asset quality concerns to aid 25bps YoY credit cost reduction in FY27E.

Performance



Source: ICE, Ambit Capital Research

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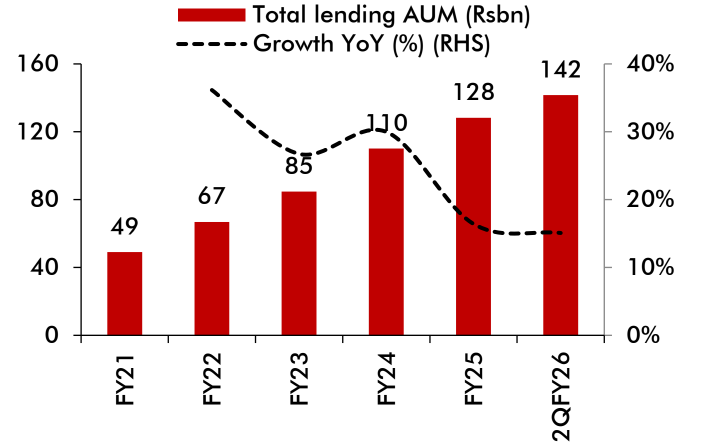
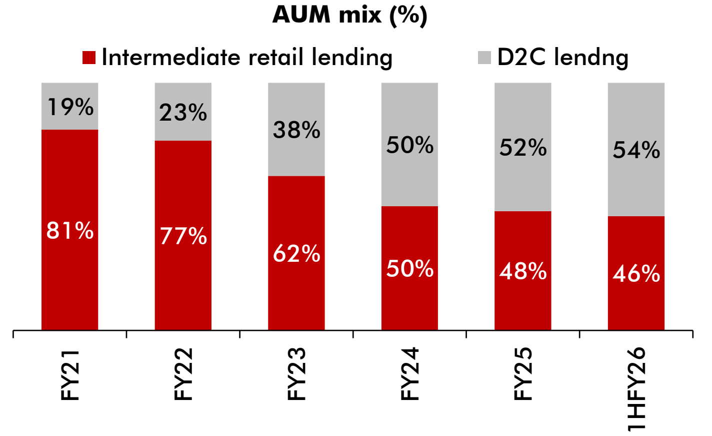
Narrative in charts

Exhibit 1: NACL has been scaling up steadily...



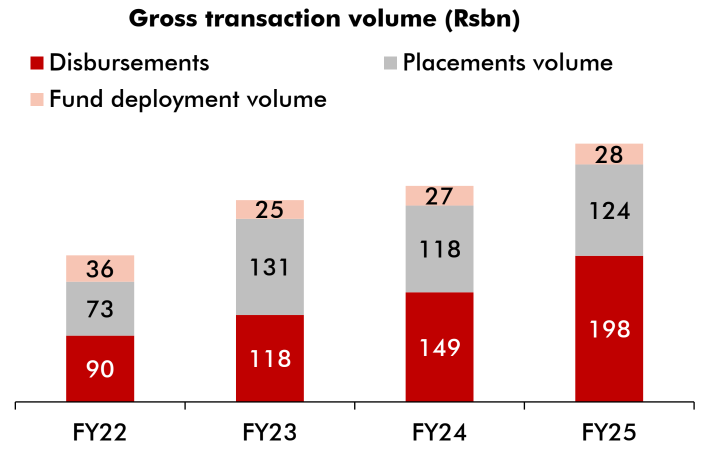
Source: Company, Ambit Capital research

Exhibit 2: ...with higher focus on high-margin D2C



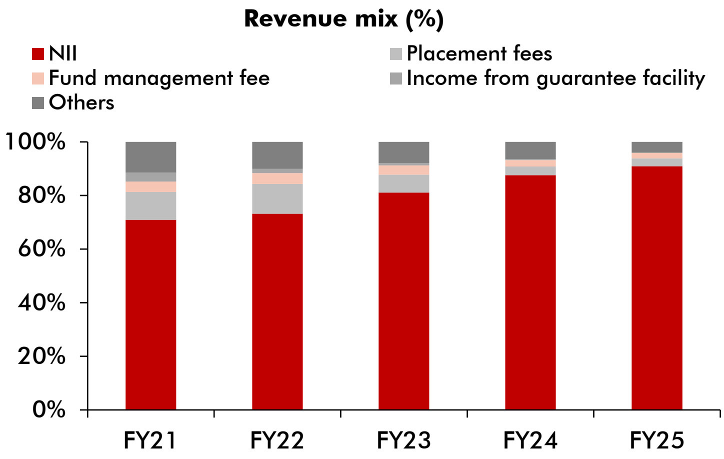
Source: Company, Ambit Capital research

Exhibit 3: Focusing on non-lending businesses too...



Source: Company, Ambit Capital research

Exhibit 4: ...to diversify revenue stream and enhance ROE



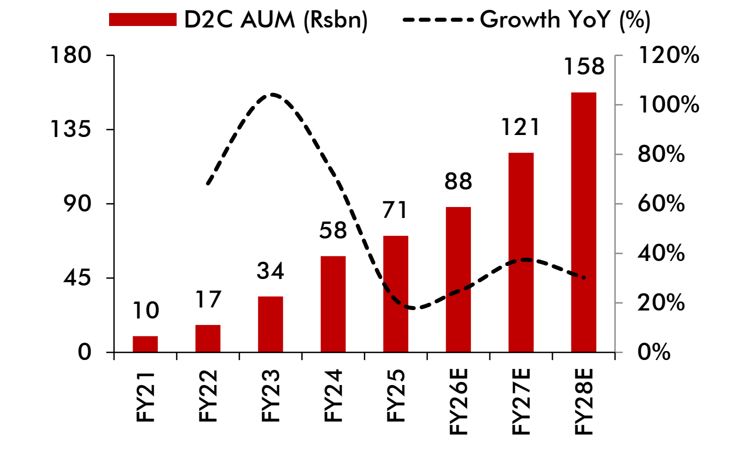
Source: Company, Ambit Capital research

Exhibit 5: Since increasing focus on D2C (retail) in FY22, profitability has improved

	FY19	FY20	FY21	FY22	FY23	FY24	FY25
Total assets growth YoY (%)	11.5%	7.5%	23.9%	40.0%	17.5%	24.9%	16.5%
ROE tree (%)							
NII (NIM)	5.2%	5.7%	5.0%	5.4%	7.0%	9.8%	11.0%
Non-interest income	2.6%	1.6%	2.0%	2.0%	1.6%	1.4%	1.1%
Net operating income	7.8%	7.3%	7.0%	7.4%	8.7%	11.2%	12.1%
Opex	3.1%	3.3%	2.5%	3.2%	4.5%	6.0%	5.8%
Operating profit	4.7%	4.1%	4.6%	4.2%	4.2%	5.2%	6.3%
Credit cost	0.4%	0.8%	2.6%	0.5%	0.5%	1.2%	3.2%
PBT	4.3%	3.3%	1.9%	3.6%	3.7%	4.0%	3.1%
Tax	1.5%	0.9%	0.5%	1.0%	0.9%	1.0%	0.7%
PAT (ROA)	2.8%	2.3%	1.5%	2.7%	2.8%	3.0%	2.4%
ROE	10.8%	7.1%	4.7%	10.4%	12.4%	14.5%	10.5%

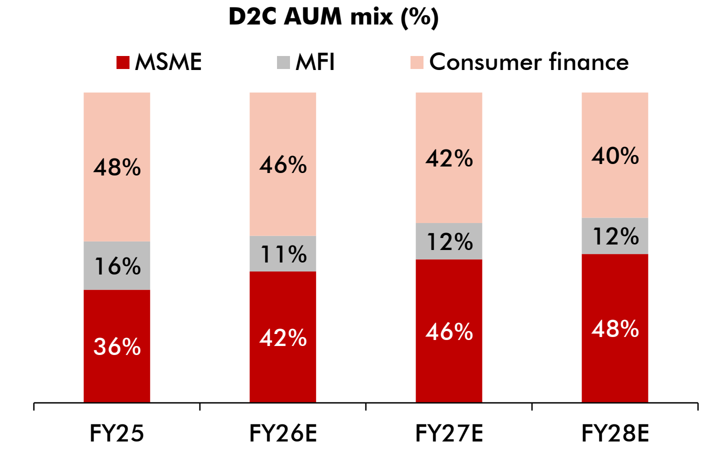
Source: Company, Ambit Capital research

Exhibit 6: D2C AUM growth to be led by revival in MSME, MFI, consumer loans as well as diversification benefits



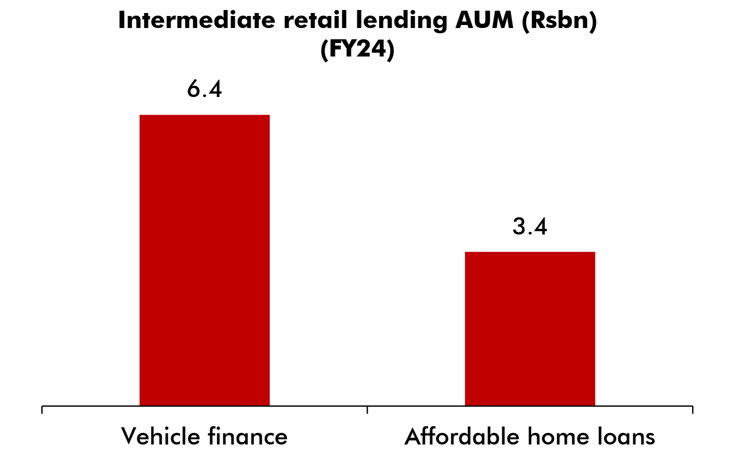
Source: Company, Ambit Capital research

Exhibit 7: MSME to lead overall AUM mix, followed by MFI and consumer finance



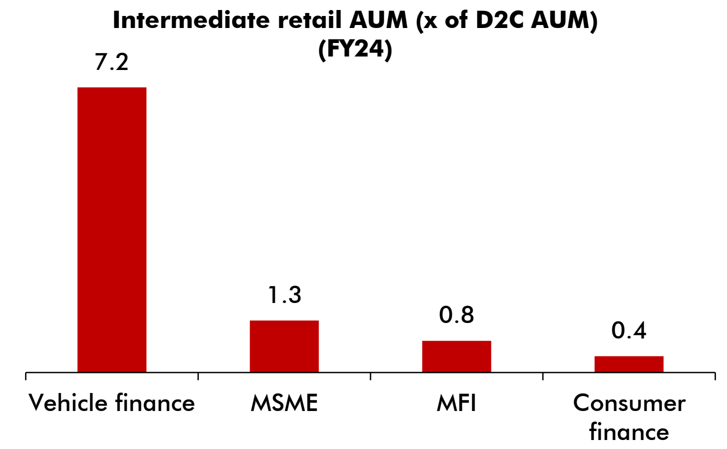
Source: Company, Ambit Capital research

Exhibit 8: Intermediate retail lending in vehicle finance and affordable home loans indicate expertise in these sectors…



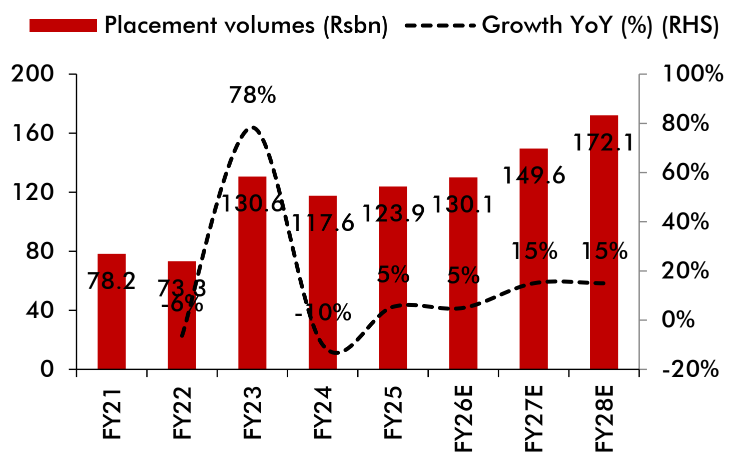
Source: Company, Ambit Capital research

Exhibit 9: …which opens up room to pursue these product opportunities in retail, which could help build scale profitably



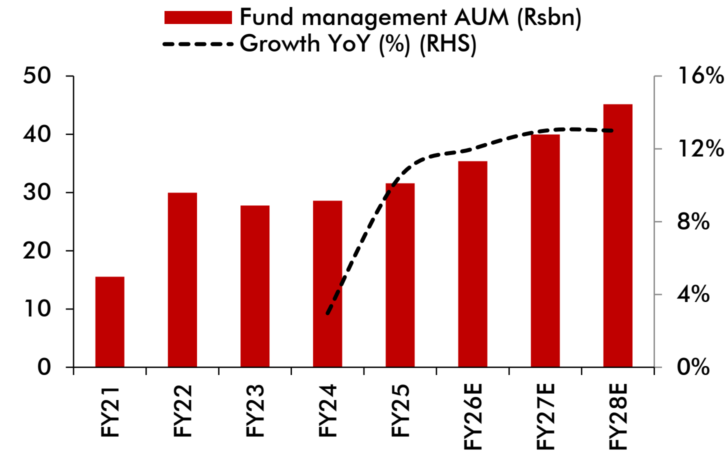
Source: Company, Ambit Capital research

Exhibit 10: Growing securitization to aid placement volumes…



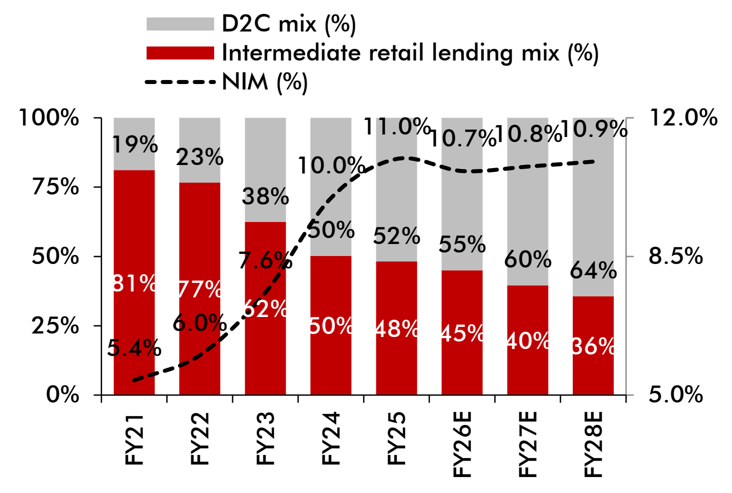
Source: Company, Ambit Capital research

Exhibit 11: …while emerging corporates' funding needs to aid fund management business



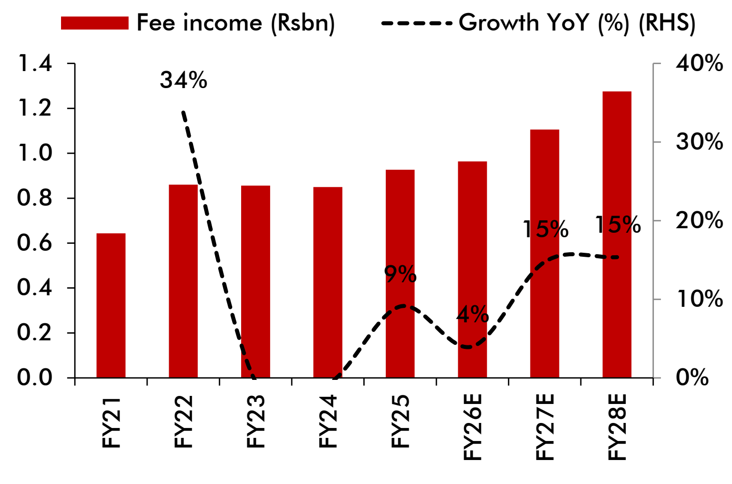
Source: Company, Ambit Capital research

Exhibit 12: Increasing D2C mix to aid stable-to-expanding NIMs and contribute towards ROA/ROE expansion



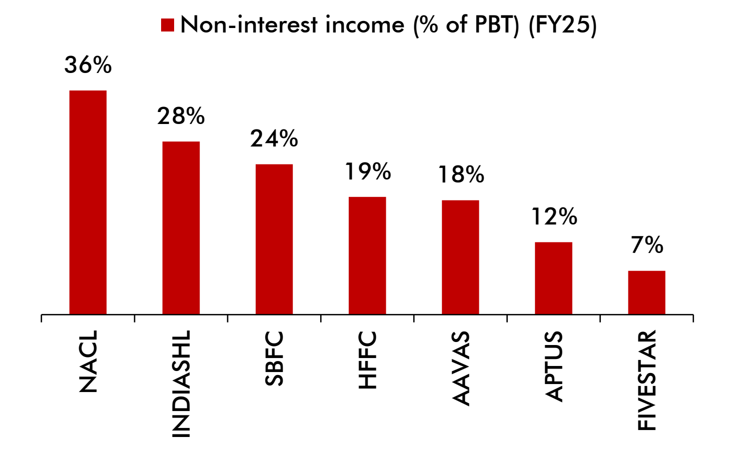
Source: Company, Ambit Capital research

Exhibit 13: Fee income aided by growing placement volumes and fund management business



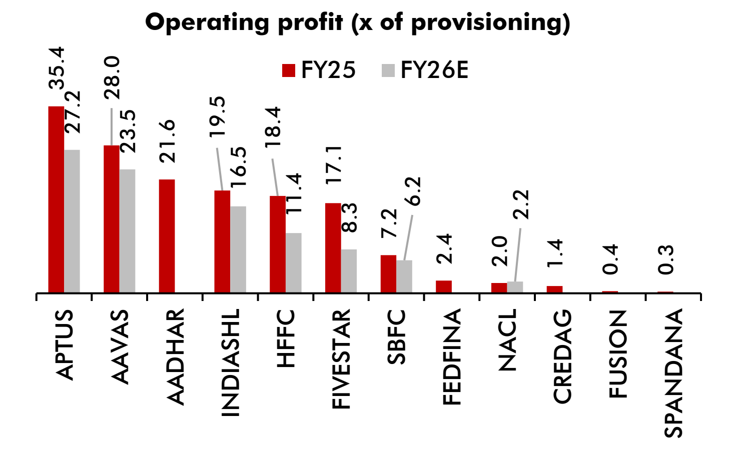
Source: Company, Ambit Capital research

Exhibit 14: Fee income from placements and fund management aid non-lending revenue lines…



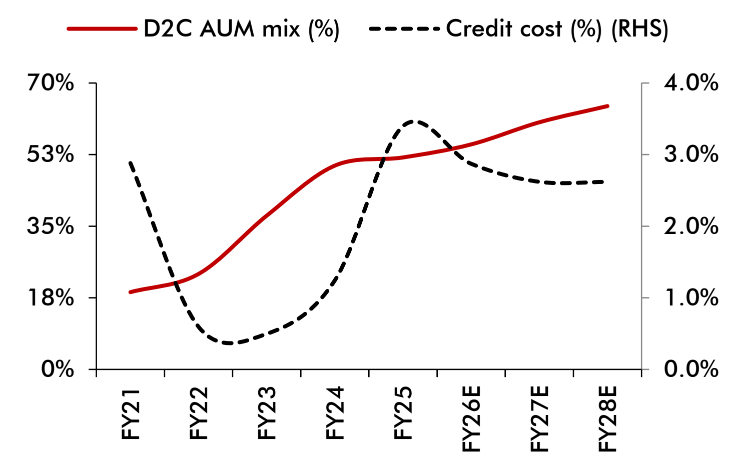
Source: Companies, Ambit Capital research

Exhibit 15: …strengthening operating profit to absorb credit losses from retail lending



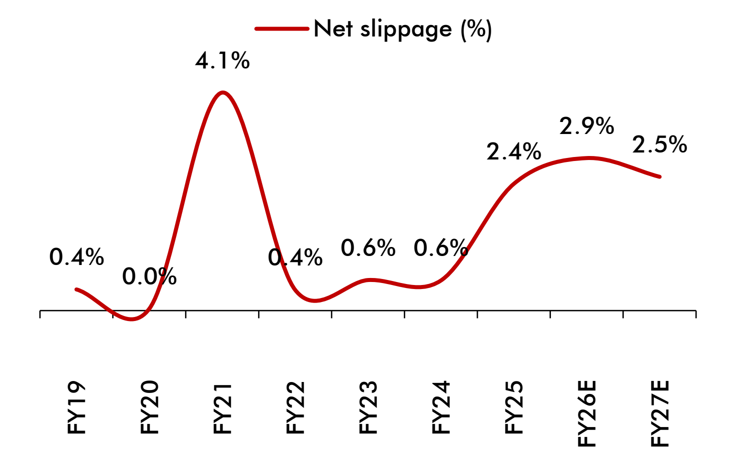
Source: Companies, Ambit Capital research

Exhibit 16: Increasing D2C to lead to higher structural credit costs but more than compensated for by higher yields



Source: Company, Ambit Capital research

Exhibit 17: Expect overall net slippages to reduce



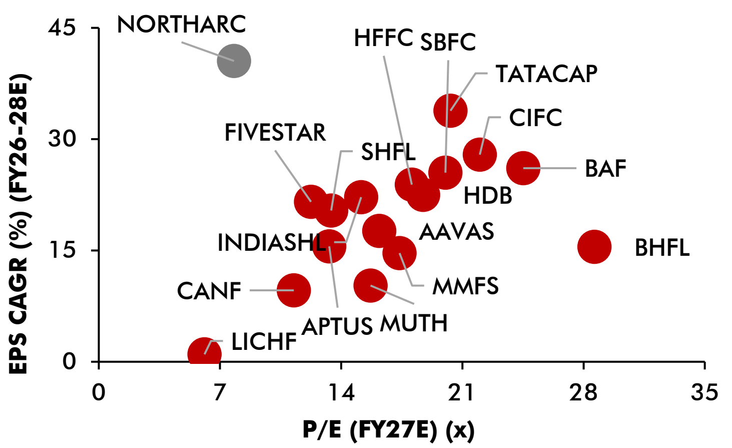
Source: Company, Ambit Capital research

Exhibit 18: AUM growth to reive, led by D2C mix, which would aid NIMs. Reducing credit costs to add to ROE expansion

Key assumptions and estimates	FY23	FY24	FY25	FY26E	FY27E	FY28E	Comments
Key assumptions							
Lending AUM growth YoY (%)	27%	30%	16%	18%	25%	22%	Growth to recover in FY27/28E on back of subsiding asset quality issues and small scale.
NIM (%)	7.6%	10.0%	11.0%	10.7%	10.8%	10.9%	Increasing D2C mix to aid margin expansion.
Non-interest income (% of assets)	1.6%	1.4%	1.1%	1.1%	1.1%	1.0%	
Opex/assets (%)	4.5%	6.0%	5.8%	5.5%	5.2%	4.8%	Increasing scale to aid opex absorption.
Credit cost (%)	0.5%	1.2%	3.4%	2.9%	2.6%	2.6%	Credit costs to subside as asset quality headwinds subside.
Estimates							
Lending AUM (₹ bn)	90.1	117.1	136.3	160.2	200.3	244.8	
PAT (₹ bn)	2.4	3.2	3.0	3.8	5.4	7.4	
ROA (%)	2.8%	3.0%	2.4%	2.5%	2.9%	3.2%	
ROE (%)	12.4%	14.5%	10.5%	10.4%	13.2%	15.7%	ROE expansion led by increasing NIMs and reducing credit costs.
EPS (₹)	25.9	34.6	20.1	23.3	33.3	46.0	
BVPS (₹)	158.6	177.5	213.1	236.2	269.5	315.4	

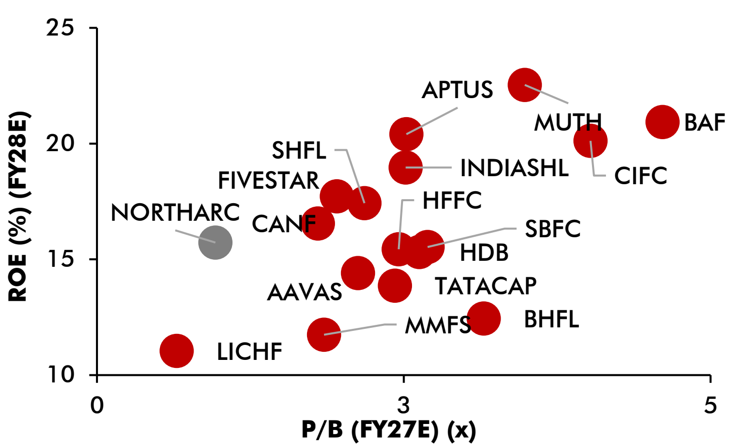
Source: Company, Ambit Capital research

Exhibit 19: Earnings growth higher vs peers led by NIM improvement and credit cost reduction...



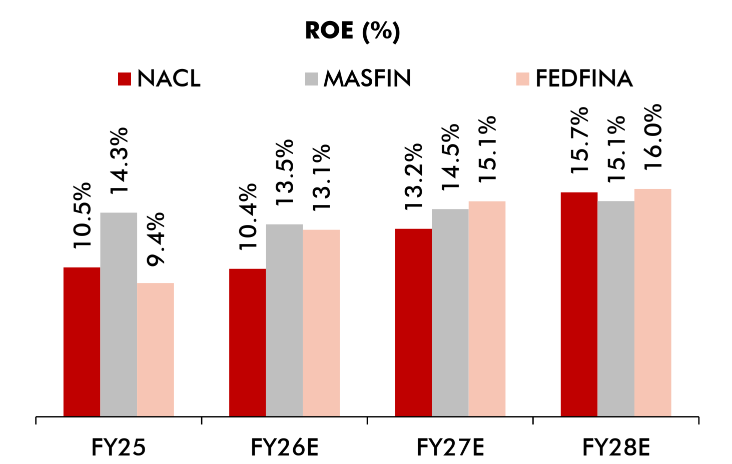
Source: Companies, Ambit Capital research

Exhibit 20: ...however, valuations undermine such recovery as reflected in 50-60% valuation discount



Source: Companies, Ambit Capital research

Exhibit 21: NACL to see higher ROE expansion/EPS CAGR led by increasing high-margin D2C mix...



Source: Visible Alpha, Companies, Ambit Capital research. Note: Consensus estimates for FEDFINA, MASFIN.

Exhibit 22: ...but trades at lower valuation multiples

Company	EPS CAGR (%) (FY26-28E)	Trailing P/B (x)	Trailing P/E (x)
NACL	41%	1.1	14.3
FEDFINA	28%	1.9	21.3
MASFIN	21%	2.1	17.1

Source: Visible Alpha, Companies, Ambit Capital research. Note: Consensus estimates for FEDFINA, MASFIN.

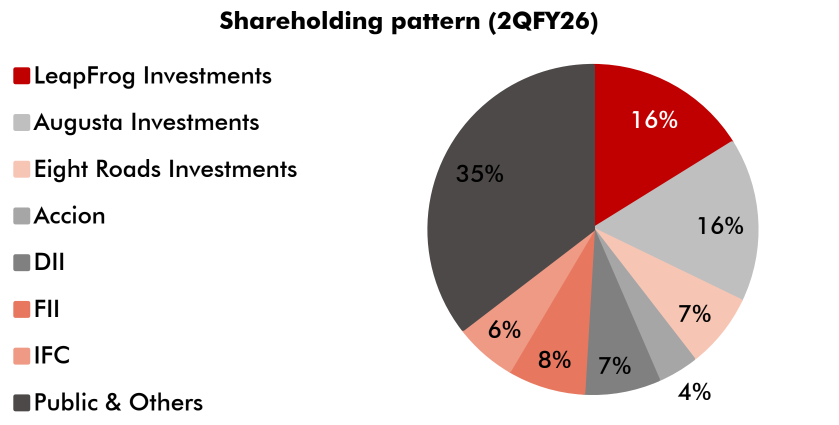
Solutions provider across NBFC ecosystem

Northern Arc Capital (NACL) formed as IFMR trust acquired an existing NBFC in 2008. Until Apri'22, when NACL acquired S.M.I.L.E to strengthen retail outreach, it had 70-80% wholesale AUM mix. Since then, NACL increased D2C (direct retail) mix to 54% as of 1HFY26. Today, it provides wholesale as well as retail credit solutions along with helping lenders with financing through placements and fund management businesses. Technology stack that integrates AI/ML-based underwriting, co-lending, credit processing and fixed income offerings to retail investors enables NACL's ecosystem approach to providing credit solutions to an expanding NBFC sector. Increased focus on D2C led to 500bps NIM expansion (FY22-25) and improved profitability given higher ROE for similar ROAs as in the past. Given MFI/MSME/consumer finance exposures in D2C, asset quality outcomes are at par with the industry, not worse.

Professionally managed, diversified financial services platform

Northern Arc Capital Limited (NACL), incorporated initially as Highland Leasing & Finance Pvt Ltd in 1989 and acquired by IFMR Trust in 2008, is a professionally managed NBFC. It is ~57% owned by foreign institutional investors. In Apr'22, NACL acquired S.M.I.L.E. Microfinance to strengthen its D2C rural reach. Over the years, NACL has transitioned from a wholesale-dominated lender to a diversified product, multi-channel NBFC, focusing on underserved households.

Exhibit 23: Majorly owned by foreign institutional investors



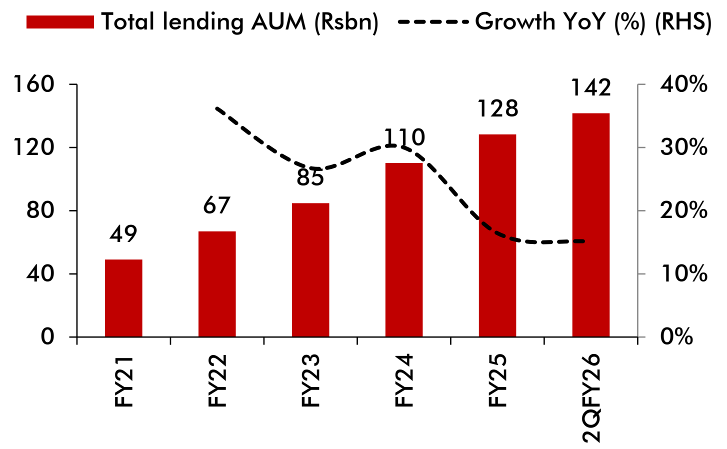
Source: Company, Ambit Capital research

Multi-channel approach to providing credit solutions

NACL caters to the credit market through 3 verticals – lending, placements and fund management.

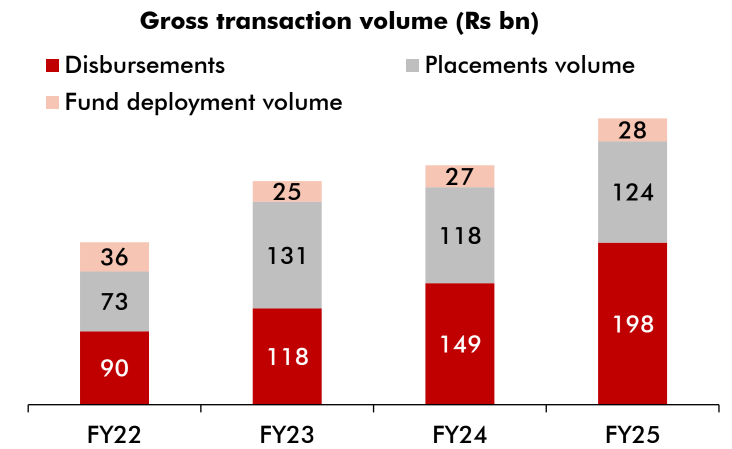
- **Lending:** In this vertical, NACL provides financing through intermediate retail lending (wholesale) and D2C (retail).
  - Intermediate retail lending is aimed at originator partners (NBFCs, HFCs and SFBs) in sectors such as MSME finance, MFI, consumer finance, vehicle finance, affordable HFCs and agri finance for on-lending by them to the underserved borrowers. NACL takes security by hypothecation of the end-borrower's assets.
  - In D2C lending, NACL provides financing directly to the retail customers through 372 branches across 14 states and 55 digital partners.
- **Placements:** NACL works with a network of investor partners to structure and syndicate debt, credit-enhanced instruments and portfolio financing for its originator partners. NACL focuses on placements where it has expertise and tracks performance on ongoing basis.
- **Fund management:** This business is operated through subsidiary Northern Arc Investment Managers, which manages six funds and 3 PMS. This business commenced operations in FY14 and has successfully exited six funds so far. Investors in this business are sourced in-house as well as through distribution partners. Domestic HNI and family-office participation is largely mobilised via external distributors.

Exhibit 24: Foray into D2C segment aided AUM growth…



Source: Company, Ambit Capital research

Exhibit 25: …along with growing non-lending lines of business such as placement and fund management



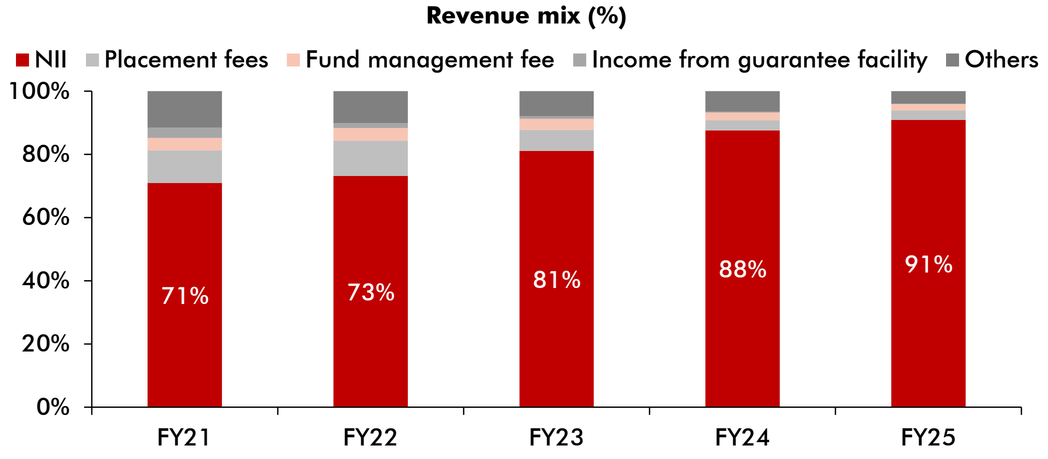
Source: Company, Ambit Capital research

Exhibit 26: Within D2C lending, product offerings are diversified across secured, unsecured segments and customer-type

D2C products	MSME (secured LAP)	Consumer finance	Rural finance/MFI
Target customers	Self-employed, wholesale & retail dealers, merchants, builders, manufacturers & service providers	Salaried & Self-employed individuals	Micro entrepreneurs in JLG format
Sourcing Channel	Direct (Branch/Digital)	Direct- Digital (23 live partners)	Direct- Branch
Security	Secured- Collateral/ FLDG	Quasi Secured- FLDG	Unsecured- CGFMU cover
Disbursement ATS	₹1.1-1.5mn	₹50k-0.5mn	₹45k
Average bureau score	600+	650+	-
Average LTV (%)	48%	-	-
Average tenure	10+ years	1-4 years	2 years

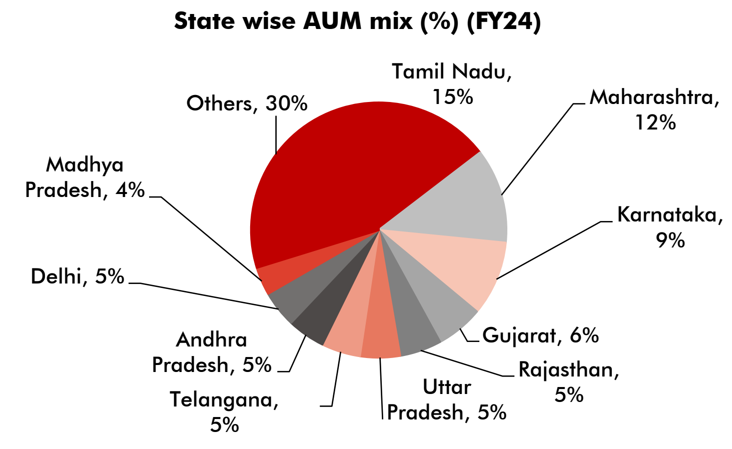
Source: Company, Ambit Capital research

Exhibit 27: Diversified revenue mix due to lending as well as non-lending businesses



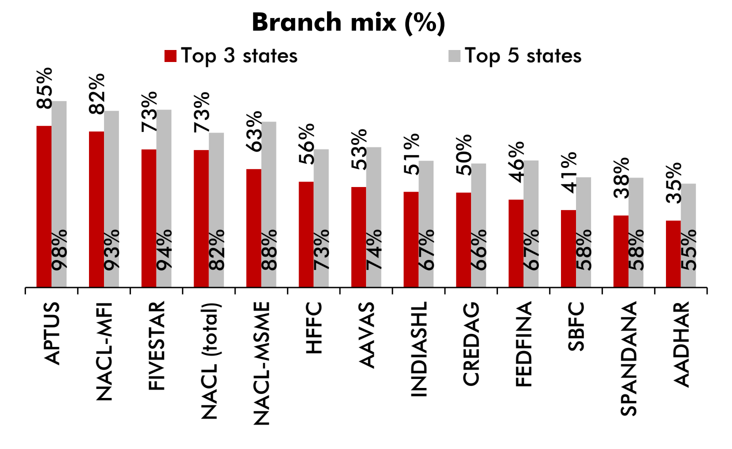
Source: Company, Ambit Capital research

Exhibit 28: NACL operates out of 7-8 states…



Source: Company, Ambit Capital research

Exhibit 29: …but given high concentration in top3/5 states, there's ample scope for diversification



Source: Companies, Ambit Capital research

Integrated tech platforms aid ecosystem approach to providing credit solutions

NACL's business model is supported by its proprietary end-to-end integrated technology platforms customized to multiple sectors.

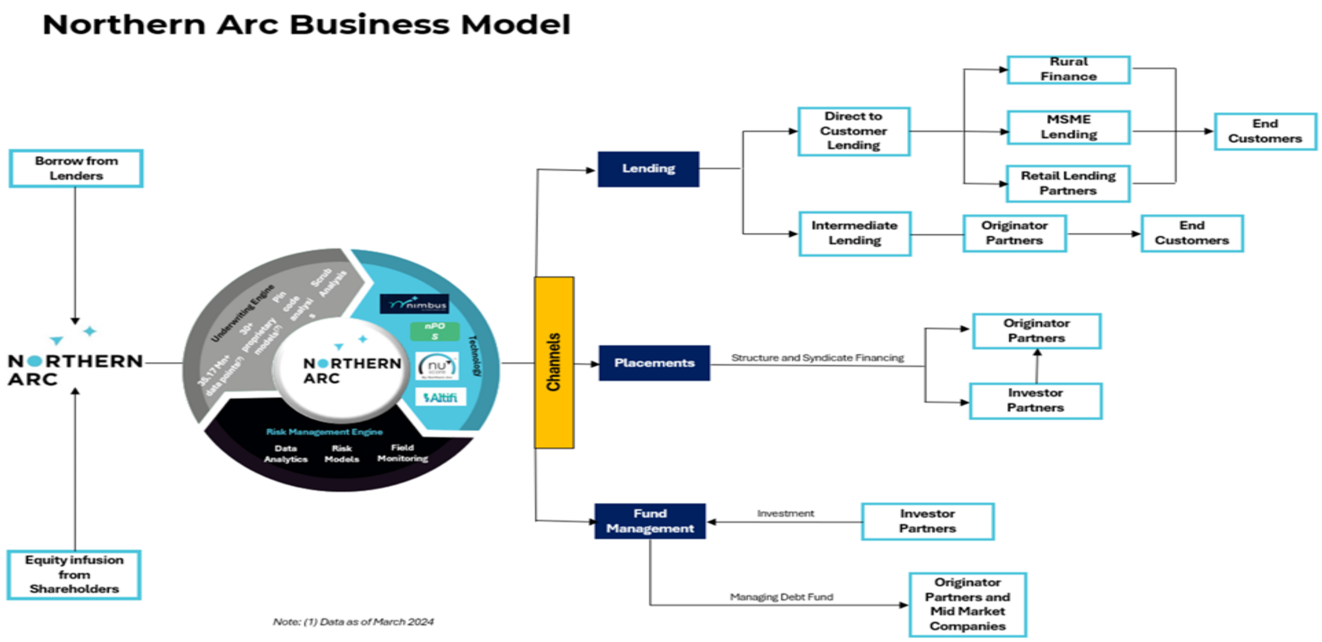
- **NuScore:** Highly customizable ML-based underwriting platform that provides real-time, data-backed risk assessments and delivers insights into borrower behavior and portfolio risk trends.
- **nPOS:** An integrated tech platform enabling end-to-end on-lending and co-lending workflows with minimal manual intervention. NACL has begun offering nPOS to other financial institutions, also.
- **Nimbus:** A debt platform enabling end-to-end processing of credit to originator partners, either through balance sheet or via investor partners. It delivers scale, precision, and transparency with faster TAT and seamless data flow for deal tracking and performance monitoring.
- **Altifi:** A digital platform offering retail investors, HNIs, and small corporates access to fixed-income products, including bonds, AIFs, and securitized assets.

Exhibit 30: Overall lending operations backed by strong technology backbone

Intermediate retail lending **Function**	**Comments**
Sourcing & pre-screening	Relationship managers identify potential partners based on sector guidelines. Pre-due diligence review is conducted to screen candidates.
Detailed due diligence	Process includes analysing operational and financial information, assessing partner's governance structures, conducting interviews (with management, operating team, promoters/equity investors), physical visits to the partner's offices and branches, meetings with the partner's borrowers.
Approval & limits	A detailed report is submitted to the Risk Team and Credit Committee. If approved, partner is onboarded and assigned an exposure limit.
Post-onboarding	Partners are subject to periodic reviews to adjust limits based on performance and needs, alongside collaboration with investor partners for financing placement.
Placement channel	Nimbus platform allows partner investors to view real-time funding needs, customize deal structures, monitor post-investment performance.
D2C lending	
Function	**Comments**
Rural finance	Digital workflow applications are integrated with lending suites such as KYC authentication, credit bureau verification, account integration, payment and collection services, credit underwriting using data analytics, geo analytics, and rule and credit engine.
MSME lending	LAP managed through physical branches through a tech-driven LOS.
	Supply chain finance relies on in-house LMS and Nimbus for high-volume, real-time validation and bank integration. A client portal allows borrowers to upload invoices and track dashboards.
	NACL offers customized working capital and term loans to mid-market corporates based on cash-flow analysis and sector insights.
Partnership-based lending	
Function	**Comments**
Collaborative model	Collaboration with retail lending partners who act as co-lenders or loan services providers through nPOS integration.
Automated underwriting	Decisions are driven by standardized digital data, proprietary ML algorithms and business rule engines.
Partner on-boarding	In addition to governance, MIS, operational and financial performance, due diligence puts emphasis on integration of technology platform of originator partner with nPOS.
Risk mitigation	Default loss guarantees, "skin-in-the-game" for co-lenders, direct borrower collections via NACH or escrow accounts.

Source: Company, Ambit Capital research

Exhibit 31: Workflow of various lines of business underscores NACL's ecosystem approach to providing credit solutions to the NBFC sector



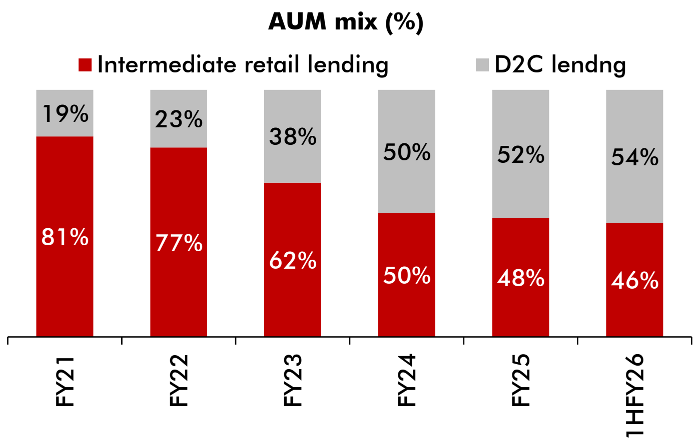
Source: Company, Ambit Capital research

Scaling up D2C segment fast

NACL's lending AUM increased at a 21% CAGR over FY18-25. In recent years, NACL accelerated its D2C strategy, leveraging capabilities built in intermediate retail lending. D2C AUM, with focus on MSME, MFI & consumer lending, increased at 64% CAGR over FY21-25, resulting in D2C AUM mix increasing to 52% in FY25 vs 19% in FY21. NACL offers D2C loans via both co-lending partnerships and direct branch-based lending.

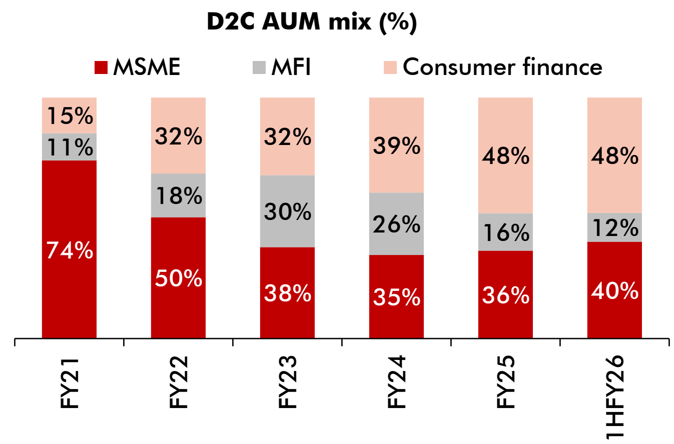
- **Partner-led origination:** NACL has a network of 55 retail lending partners (NBFCs, digital lenders, payment fintechs, merchants) through which NACL offers secured and unsecured MSME loans, MFI loans, personal loans and vehicle loans.
- **Rural lending expansion:** This is housed under Pragati (set up in FY21). Through acquisition of S.M.I.L.E Microfinance in Apr'22, NACL strengthened its rural reach (284 branches).
- **Direct MSME:** NACL has also expanded MSME through direct/in-house sourcing efforts (88 branches) in LAP (introduced in FY22) and supply chain financing (FY23).

Exhibit 32: Strategy change towards higher retail focus reflected in D2C mix increasing



Source: Company, Ambit Capital research

Exhibit 33: Diversification within D2C to capture various segments of the NBFC segment

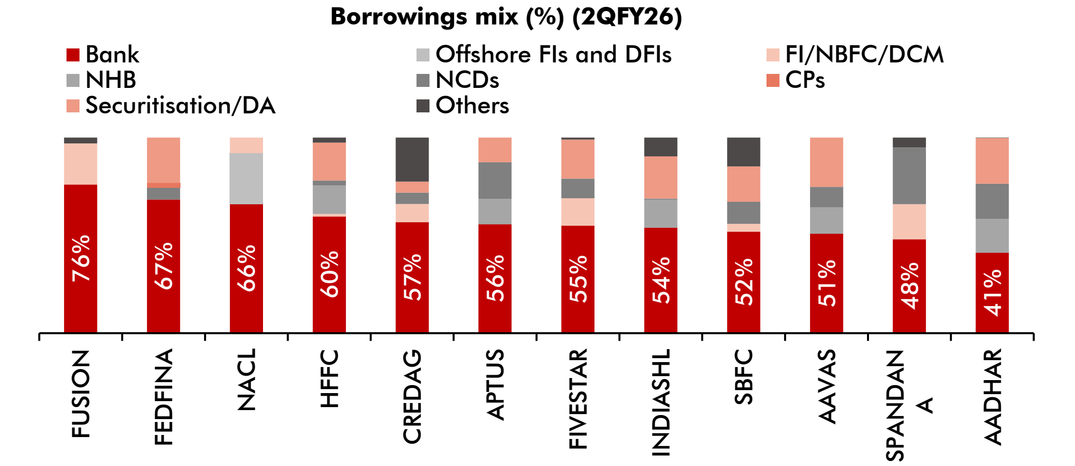


Source: Company, Ambit Capital research

Liability profile at par with peers. D2C transition aiding NIM expansion.

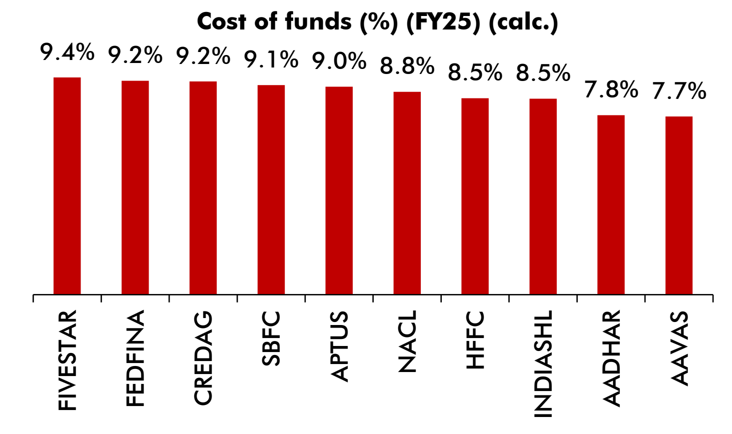
NACL's cost of funds is at par with or lower than other MSME-focused NBFCs/MFI but higher than affordable HFCs. Note that affordable HFCs have the benefit of borrowing low-cost funds from NHB, which is not available to NBFCs. Liability mix too is in line with peers given dependency on bank borrowings. NACL makes a 9.5% spread in D2C lending, where it earns interest income directly from the retail customer. This spread is higher than the 3.4-3.5% spread earned under wholesale-oriented intermediate retail lending. As NACL's lending AUM mix has increased in favour of D2C, its spreads/NIM have expanded 672bps over FY19-25.

Exhibit 34: Liability mix dependent on bank borrowings, in line with peers



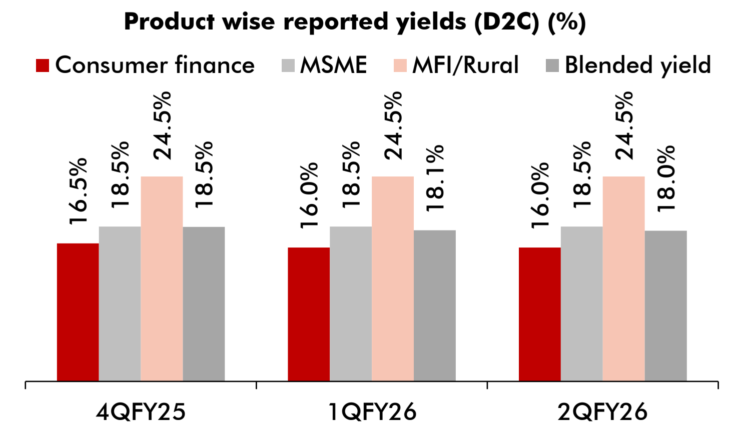
Source: Companies, Ambit Capital research

Exhibit 35: Cost of funds is competitive when compared to peers



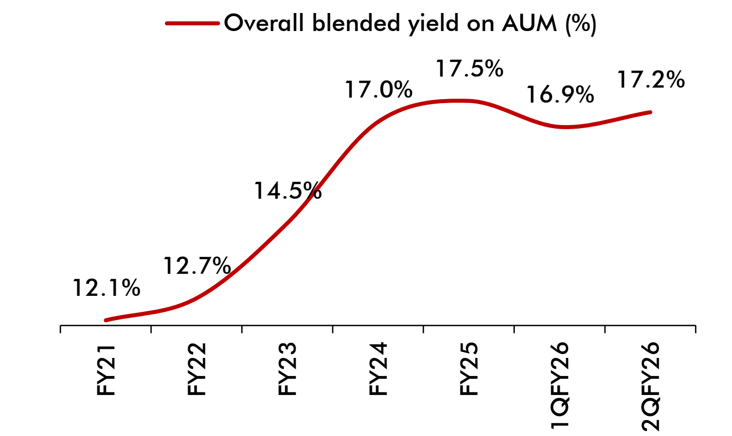
Source: Companies, Ambit Capital research

Exhibit 36: Yields are higher in D2C than in intermediate retail lending due to direct retail exposure



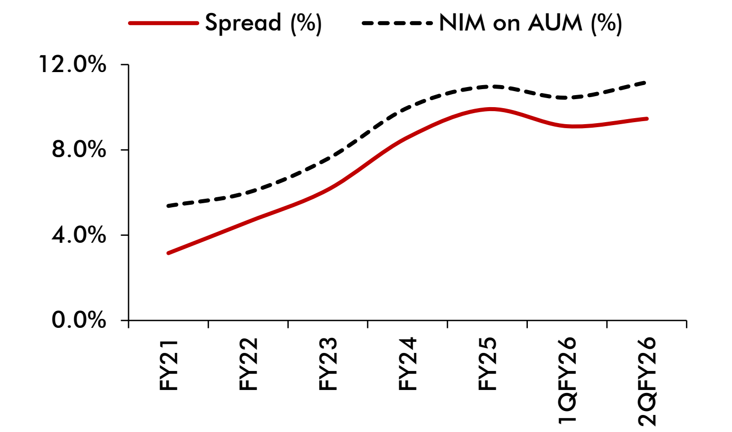
Source: Company, Ambit Capital research

Exhibit 37: The increasing D2C mix has aided yield expansion, in line with management's strategy...



Source: Company, Ambit Capital research

Exhibit 38: ...leading to expansion in spreads/NIMs

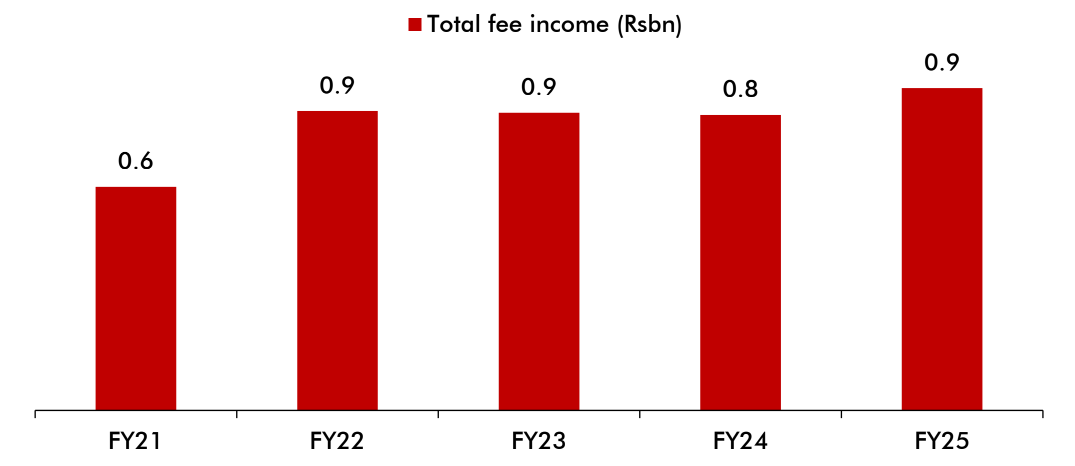


Source: Company, Ambit Capital research

Fee-generating businesses

In addition to generating interest income, NACL also earns fee income through its placements business and fund management business. These revenue streams help in diversifying the overall revenue profile and contribute towards ROE.

Exhibit 39: Placement and fund management businesses have aided fee income, thus supporting overall revenues

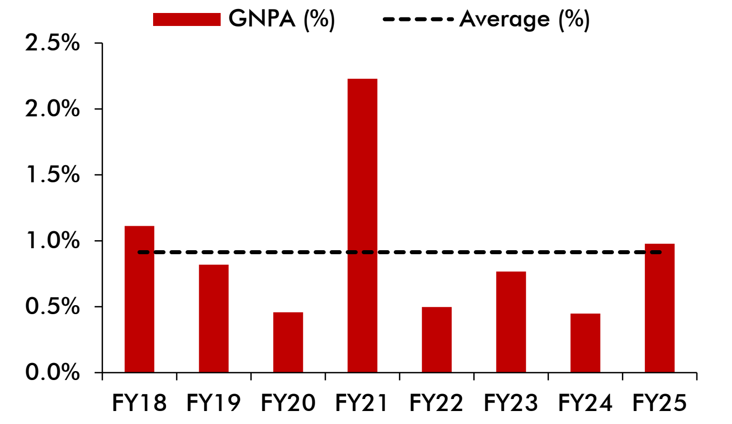


Source: Company, Ambit Capital research

Intermediate retail lending is not concerning; retail asset quality impacted due to cycle

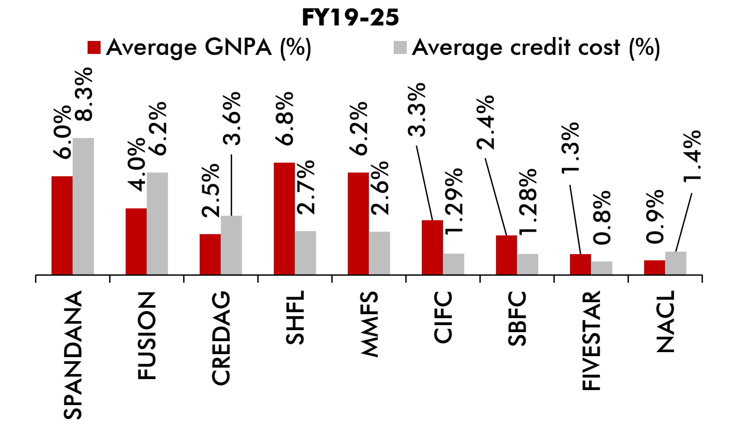
Over FY19-25, NACL has demonstrated a lower average credit cost of 1.4% vs 0.8%-8.3% for peers (MFIs, AHFCs, and MSME NBFCs). In intermediate lending, NACL secures loans to originator partners by taking exposures created through on-lending as collateral. However, asset quality in the D2C segment (direct retail) has been impacted by the cyclical downturn in the microfinance and MSME segments. As a result, D2C credit costs were 1.8-6.4% in 1HFY26 vs 1% for intermediate retail lending. Provisioning policies appear reasonable given 1.9%/25%/61% stage 1/2/3 coverage and a 90-day write-off policy. While building out the D2C portfolio, NACL is also undertaking investments in product-specific collections and underwriting staff.

Exhibit 40: Average GNPAs over a cycle at <1%...



Source: Company, Ambit Capital research

Exhibit 41: ...and average credit cost through the cycle is lower vs peers indicating reasonable underwriting



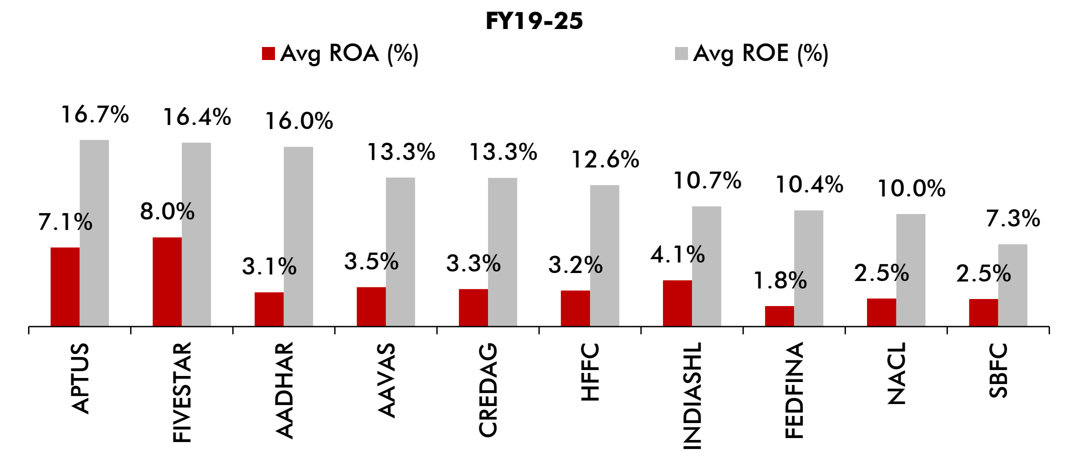
Source: Companies, Ambit Capital research

NACL has a multi-layered collection setup comprising an in-house call centre, on-field collectors, agency managers and a dedicated legal team. For stressed exposures from Originator Partners, it follows an active workout strategy where, if required, NACL can assume control of underlying loan pools offered as security and drive recoveries through collection agencies and partner network.

ROE weighed down by higher mix of low spread intermediate retail lending

NACL average ROE of 10% over FY19-25 has been sub-par vs peers due to lower spread/NIM in intermediate retail lending and also due to lower leverage of 3x. However, since it started scaling up the D2C mix in overall lending AUM, the operating profit margin has been expanding. But this benefit has been partly offset by high credit costs in FY21 and FY24/25 due to systemic stress in key segments (mainly MFI).

Exhibit 42: Historically, NACL's ROE have been weighed down by higher mix of intermediate retail lending where spreads are 3-3.5% vs 9-10% in D2C



Source: Companies, Ambit Capital research

Exhibit 43: Increasing D2C mix led to improved profitability given higher ROE for similar level of ROA as in the past (FY19/20)

	FY19	FY20	FY21	FY22	FY23	FY24	FY25
Total assets growth YoY (%)	11.5%	7.5%	23.9%	40.0%	17.5%	24.9%	16.5%
ROE tree (%)							
NII (NIM)	5.2%	5.7%	5.0%	5.4%	7.0%	9.8%	11.0%
Non-interest income	2.6%	1.6%	2.0%	2.0%	1.6%	1.4%	1.1%
Net operating income	7.8%	7.3%	7.0%	7.4%	8.7%	11.2%	12.1%
Opex	3.1%	3.3%	2.5%	3.2%	4.5%	6.0%	5.8%
Operating profit	4.7%	4.1%	4.6%	4.2%	4.2%	5.2%	6.3%
Credit cost	0.4%	0.8%	2.6%	0.5%	0.5%	1.2%	3.2%
PBT	4.3%	3.3%	1.9%	3.6%	3.7%	4.0%	3.1%
Tax	1.5%	0.9%	0.5%	1.0%	0.9%	1.0%	0.7%
PAT (ROA)	2.8%	2.3%	1.5%	2.7%	2.8%	3.0%	2.4%
ROE	10.8%	7.1%	4.7%	10.4%	12.4%	14.5%	10.5%

Source: Company, Ambit Capital research

Board and management profile

Exhibit 44: Management team led by experienced industry people

Name	Designation	Background/work experience	Total work experience (years)	Experience with NACL (years)
Ashish Mehrotra	MD & CEO	MBA from the Institute of Management Studies, DAVV, Indore and has also successfully completed the senior executive leadership program at Harvard Business School. Previously, he was the MD & CEO of Max Bupa Health Insurance Co. Ltd. and has held various positions at Citibank N.A., including MD and retail bank head, in India.	25+	4.5
Pardhasaradhi Rallabandi	Group Risk Officer & Governance Head	Bachelor of Technology degree from Nagarjuna University and a post-graduate diploma in management from IIM, Calcutta. He has been a banker at Standard Chartered Bank. He has also worked at Allahabad Bank, Global Trust Bank Limited and IDBI Bank.	31+	7.5
Gaurav Mehrotra	Chief Technology Officer	B.Tech. from the IIT, Delhi. Previously, he was the vice president, engineering in the Information Technology Department at Dhani Stocks Ltd. He has also worked at Innoviti Payment Solutions Pvt Ltd, J.P. Morgan and Goldman Sachs.	26+	3.4
Sandeep Singh	Head – Intermediate Retail	MBA from IIM, Ahmedabad. Previously, he has worked with Fitch Ratings India Pvt Ltd, where he held the position of Senior Director & Head - Structured Finance.	25+	5.3
Atul Tibrewal	CFO	Bachelor's in commerce from Calcutta University and is also an associate member of ICAI. He has worked as an assistant manager at Magma Leasing Ltd and he was a senior vice president and head of treasury at Magma Fincorp Ltd.	22+	4.6
Jagadish Babu Ramadugu	MD & CEO - Pragati	Post-graduate diploma in management from IIM, Ahmedabad. Previously, he was the MD & CEO of Vaya Finserv Pvt Ltd. He has also worked with Satyam Infoway Ltd, Hindustan Coca-Cola Beverages, Spencer's Retail and Asian Paints. He was elected as a member on the board of the MFIN where he served as the chair of the credit bureau task force and was member of its self-regulatory organisation committee and the fintech committee.	28+	5.0
Chetan Tivary	Chief Internal Audit Officer	CA with in-depth expertise in audit and risk management within the banking sector across India and the UAE. Previously, he has worked with Ujjivan SFB, Mashreq Bank, DCB Bank, ABN AMRO Bank N.V.	30+	0.7
Prakash Panda	Company Secretary	Bachelor's degree in commerce from Utkal University and a bachelor's degree in law from Fakir Mohan University. He is an associate member of ICSI and is a junior associate member of the IIB. Previously, he was associated with Tamilnad Mercantile Bank Ltd, Apollo Sindoori Hotel Ltd, ETL Power Services Ltd and Binani Industries Ltd.	16+	1.7
Saurabh Jaywant	Chief Legal Officer	Bachelor's degree in arts and law from the National Law School of India University. Previously, he worked at ICICI Bank.	22+	13.3
Amit Mandhanya	Chief Business Officer – Partnership-Based Lending	Post Graduate Programme in Rural Management course from the Institute of Rural Management, Gujarat. He was previously associated with Micro-Credit Ratings International Limited and with IOCL.	17+	12.9
Bhavdeep Bhatt	CEO - Northern Arc Investment Managers	Master's degree in business administration degree from Bhavnagar University, Gujarat. Previously, he was associated with Aditya Birla Sunlife AMC Limited as 'Head - Alternate and PMS Sales'.	29+	1.6
Priyashis Das	CEO - Northern Arc Securities	MBA from University of Calcutta and Post Grad Diploma from IIM Calcutta. Previously, he has worked with DBS, Citibank, ABN and Tata AIA.	25+	1.8
Moushumi Mandal	Deputy Chief People Officer	Master of Management Studies from University of Mumbai. Previously, she was associated with NSE, Citi Bank, JPMorgan Chase.	25+	1.9
Vipin G S	Chief Compliance Officer	Previously associated with Manappuram Finance.	24+	1.3

Source: Company, Ambit Capital research

Exhibit 45: Board led by ex-PSU CEO, supported by experienced independent direct

Name	Designation	Background/work experience	On the Board since (years)
P S Jayakumar	Chairman & Independent Director	CA and holds a master's degree from the University of Madras and a post-graduate diploma in business management from Xavier Labour Relations Institute, Jamshedpur. Previously, he worked at Citibank N. A. and has also served as the MD & CEO of VBHC Value Home Pvt Ltd and Bank of Baroda.	5.2
Ashish Mehrotra	MD & CEO	MBA from the Institute of Management Studies, DAVV, Indore and has also successfully completed the senior executive leadership program at Harvard Business School. Previously, he was the MD & CEO of Max Bupa Health Insurance Co. Ltd. and has held various positions at Citibank N.A., including MD and retail bank head, in India.	3.8
Ashutosh Arvind Pednekar	Independent Director	Bachelor's degree in commerce from University of Bombay. He has been a practising chartered accountant for over 30 years.	5.3
Sandeep Dhar	Independent Director	He holds a Bachelor's degree from Delhi University, a Post Graduate Diploma in Business Management from IMT, Ghaziabad, and has completed an Advanced Management Programme at the Wharton Business School. He is a seasoned professional with experience in the BFSI sector and IT services.	0.6
Vidya Krishnan	Independent Director	Bachelor's degree and MBA from University of Mumbai. She is also a Certified Associate of the IIB. She has expertise in banking, IT, digital transformation, and business leadership across retail, wholesale, and investment banking, along with deep experience in managing relationships with government bodies, regulators, and global CXOs.	0.1
Anuradha Rao	Non-Executive Non-Independent Director	Master's degree from the University of Hyderabad. She has 36 years of experience in banking and finance and has worked at SBI. She also served as the MD & CEO of SBI Funds Management Pvt Ltd.	6.1
Kshama Fernandes	Non-Executive Non-Independent Director	Master's degree and PhD in management studies from Goa University. She has 25+ years of experience across management, risk advisory and academia. She is a financial risk manager certified by GARP. Previously, she was a professor at the Goa Institute of Management and has also served as CRO and MD of NACL.	13.4
Michael Jude Fernandes	Non-Executive Nominee Director	Post-graduate diploma from the IIM, Calcutta. He co-leads the LeapFrog group's investments in South and Southeast Asia, with 20 years of experience in consulting and investing. He was formerly an ED at Khazanah India Advisors Pvt Ltd, the sovereign fund of Malaysia and served on the boards of IDFC Limited and Apollo Hospitals Enterprise Ltd. He has been an ED at Piramal Enterprises and was a partner with McKinsey & Co.	11.7
Vijay Chakravarthi	Non-Executive Nominee Director	MBA from the J. L. Kellogg School of Management, Northwestern University. He is currently Partner at Affirma Capital India and formerly was an ED, private equity at Standard Chartered Bank. He is involved with Affirma's investments in certain portfolio companies.	7.9

Source: Company, Ambit Capital research

SWOT – NACL's technology strength and diversified nature offer scalability opportunities but we also remain watchful of concentration risks

Strengths

- **Diversified revenue mix:** Multiple income streams - interest income & high RoE fee income provide earnings stability. Fee income contribution to PBT is higher vs peers.
- **Leveraging IR lending:** Deep experience with originating partners strengthens high-yield D2C portfolio expansion.
- **Distribution:** Large ecosystem of 372 branches, 55 digital partners, 357 originating partners, 1400+ Investor partners aid scale.
- **Proprietary tech platforms:** Technology stack empowers offers diverse financial services and enhances underwriting, data insights and scalability.

Weaknesses

- **Regional concentration:** 75% of branches are in South India, limiting geographic diversification and exposing to any geography-specific concern.
- **High-risk customer profile:** Focus on bottom-of-the-pyramid borrowers increases credit quality vulnerability.
- **Partner dependence:** IR lending concentration (46% lending AUM mix) exposes NACL to partner-level operational/financial risks.

Opportunities

- **MSME credit gap:** CRISIL Intelligence estimates total addressable MSME credit gap of ~₹34tn (FY25), presenting strong lending runway.
- **Pan-India scale-up:** Branch expansion beyond South-India offers huge market opportunity and can accelerate AUM growth.
- **Product diversification:** Expanding into adjacent sectors such as climate lending, gold loan, vehicle finance, and affordable home loans offers growth.

Threats

- **Rising competition:** Increasing competition from MFIs/NBFCs/banks may limit AUM growth and put pressure on margins.
- **Employee attrition:** D2C business is manpower- intensive. Higher employee turnover due to competition could impact AUM growth/asset quality.
- **Macro & state-specific issues:** External shocks (Covid, demonetization, over-leveraging) in MSME/MFI segment and state-specific issues (Andhra Pradesh, Karnataka, Tamil Nadu state bill) can dent operations.
- **PE ownership may restrict ratings:** High PE ownership can restrict ratings due to the possibility of a change in ownership.

Source: Company, Ambit Capital research

D2C pivot for scale, expanding NBFC sector to aid intermediate lending

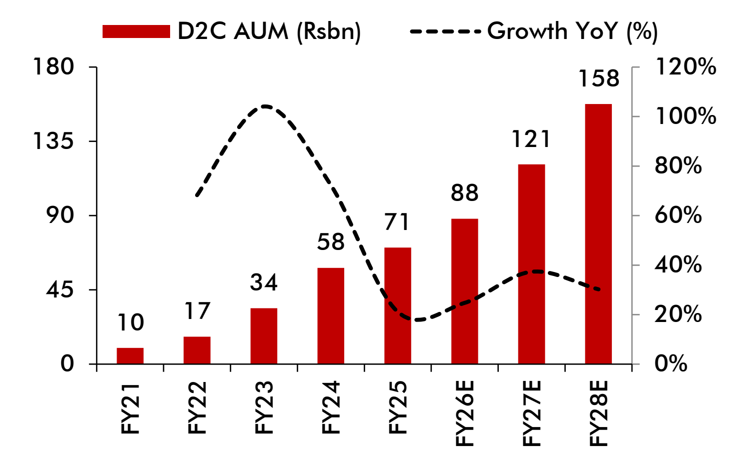
NACL's D2C pivot is expected to continue with D2C AUM increasing at 34% CAGR (FY26-28E) and D2C AUM mix increasing to 64%. D2C scale-up would be supported by a diversified asset mix, given presence across secured/unsecured MSME loans, MFI, consumer finance and expanding distribution. Having done vehicle and affordable home finance through intermediate retail lending, NACL has the required expertise to scale up these segments in retail format, indicating additional levers for long-term scale. NBFC sector's borrowing requirements (FY26-28E: 18% CAGR) should aid intermediate retail lending AUM CAGR of 10% (FY26-28E) and fee-generating placement volumes (12% CAGR). We expect overall lending AUM to increase at 24% CAGR (FY26-28E).

High growth potential in D2C segments

NACL's management has undertaken a shift towards increasing D2C (direct retail) as this segment is ROE-accretive vs intermediate lending. Within D2C, there is immense growth potential across sub-segments, especially considering NACL's minuscule market share.

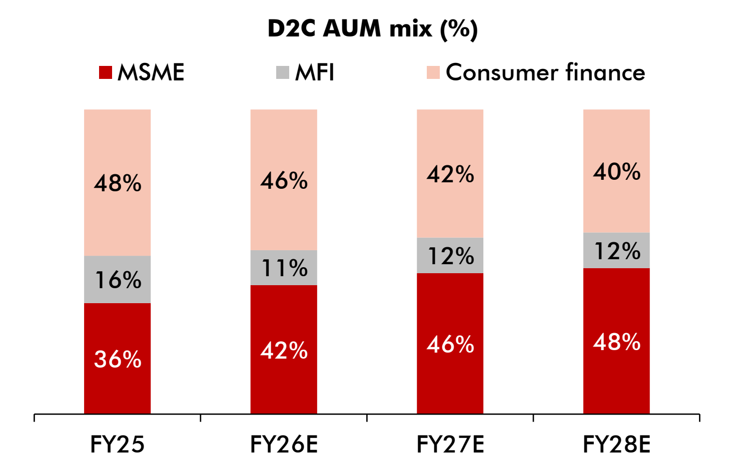
- Our findings and insights from studying Five-Star and SBFC (BUYs) indicate that small ticket LAP has low competition due to high operational intensity involved in underwriting and collections in this product.
- Supply chain financing, a sub-segment of MSME segment, has seen 18-19% CAGR (FY20-25). As per CRISIL, supply chain financing is expected to increase at 12-14% CAGR (FY25-28). NACL's ecosystem approach to growth aids higher-than-industry growth in this segment.
- With over-leveraging and asset quality concerns abating in MFI segment, NACL's growth in MFI segment should recover to 35% CAGR (FY26-28E).
- Growth in consumption finance to be supported by digital partnerships, FLDG and evolving consumption patterns.
- Overall, we expect D2C portfolio to grow at 34% CAGR (FY26-28E).

Exhibit 46: D2C AUM grow to be led by revival in MSME, MFI, consumer loans as well as diversification benefits



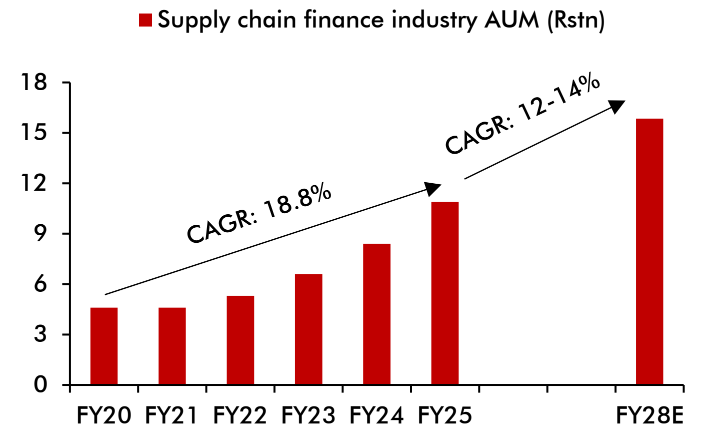
Source: Company, Ambit Capital research

Exhibit 47: MSME to lead overall AUM mix, followed by MFI and consumer finance



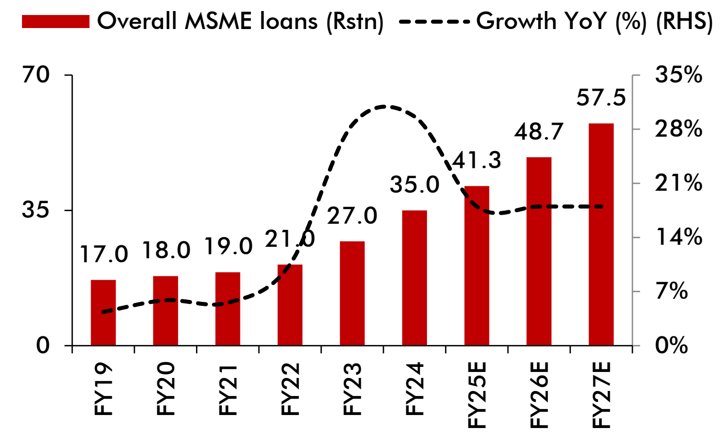
Source: Company, Ambit Capital research

Exhibit 48: Supply chain finance growth opportunity pegged at 12-14% over FY25-28E



Source: CRISIL, Ambit Capital research

Exhibit 49: CRISIL estimates overall MSME credit to grow at 18% CAGR

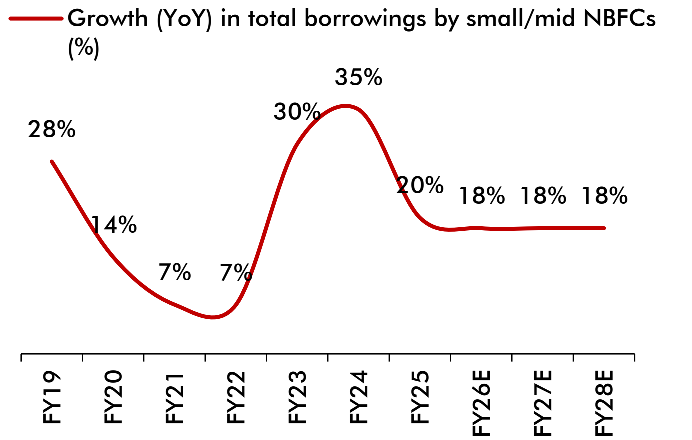


Source: CRISIL, Ambit Capital research

Expanding NBFC sector to aid growth in intermediate lending portfolio and placement volumes

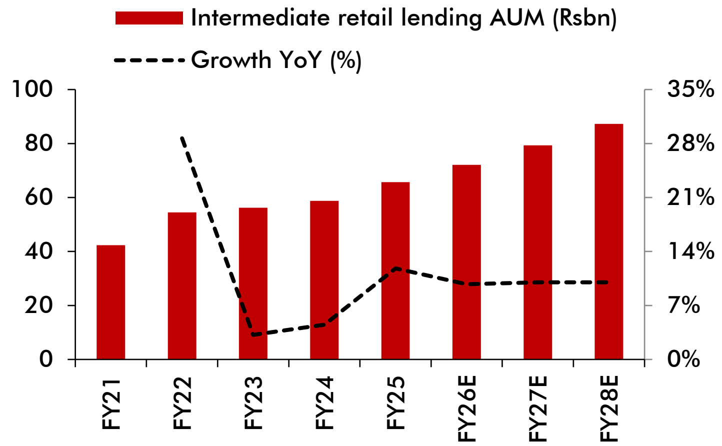
Aggregate data for 40 sub-scale NBFCs show that their borrowing requirements have grown at an 18% CAGR over FY19-25. The NBFC sector is poised to grow at 18-19% over the next 1-2 years, according to Crisil. Assuming a 15% long-term CAGR in the NBFC sector's borrowing requirements and given NACL's emphasis on fee-generating placement volumes, we are building NACL's intermediate lending portfolio to grow at ~10% CAGR (FY26-28E).

Exhibit 50: Financial inclusion to drive NBFC sector expansion and their borrowing needs...



Source: Ambit Capital research. Note: For estimating borrowings by small/mid-size NBFCs, we have considered data for 40 NBFCs. For FY26/28E, we have assumed 18% CAGR in borrowings.

Exhibit 51: ...leading to growth opportunities for intermediate retail lending for NACL

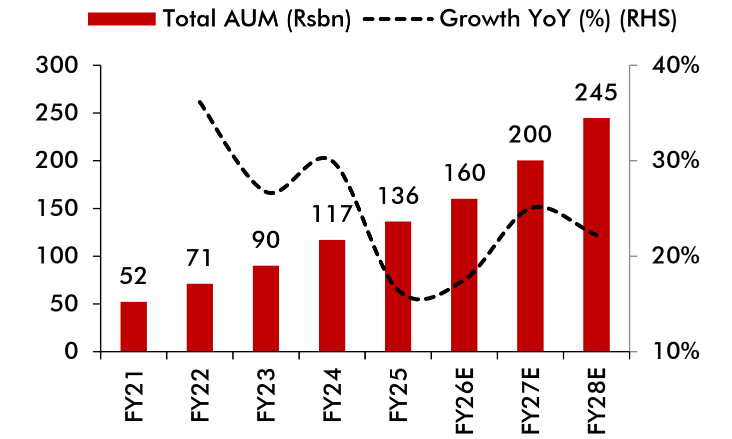


Source: Company, Ambit Capital research

Multiple channels to aid 24% AUM CAGR (FY26-28E)

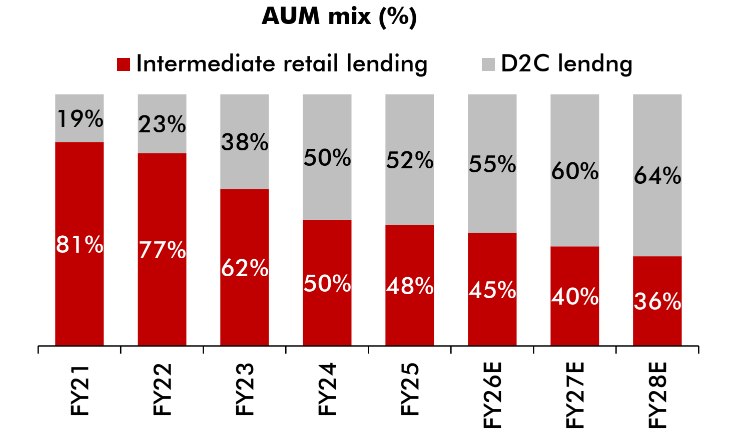
We expect overall lending AUM to increase at a 24% CAGR (FY26-28E), driven by higher growth in D2C, in line with management strategy, as well as by the revival in bottom-of-the-pyramid lending. Given NACL's D2C pivot, we expect 25 new branches annually, which should support direct-sourcing efforts. That said, greater geographical diversification (vs. the current mix) would help capture the pan-India growth opportunity.

Exhibit 52: Overall lending AUM growth to be led by higher growth in D2C portfolio



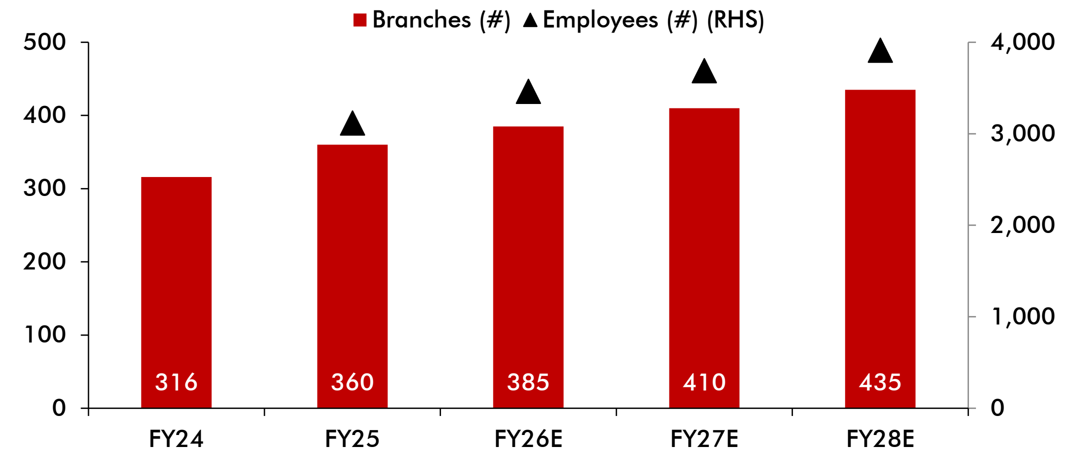
Source: Company, Ambit Capital research

Exhibit 53: Increasing D2C mix to be led by MFI/MSME loans, while intermediate growth would be supported by expanding NBFC sector



Source: Company, Ambit Capital research

Exhibit 54: D2C focus to be supported by branch expansion

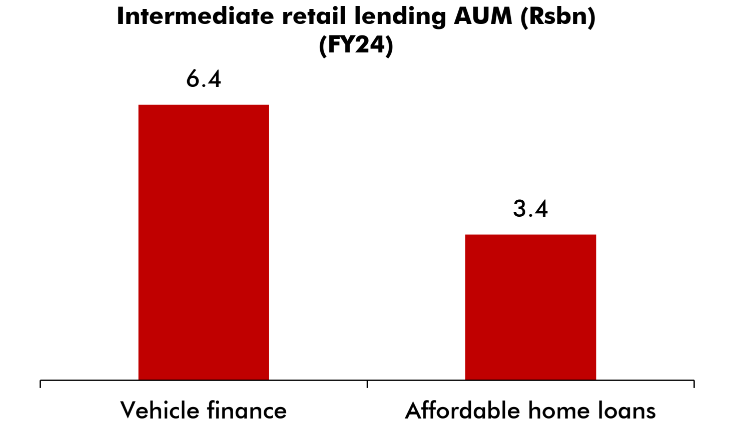


Source: Company, Ambit Capital research

Vehicle & affordable mortgage finance expertise can add to scale and diversification

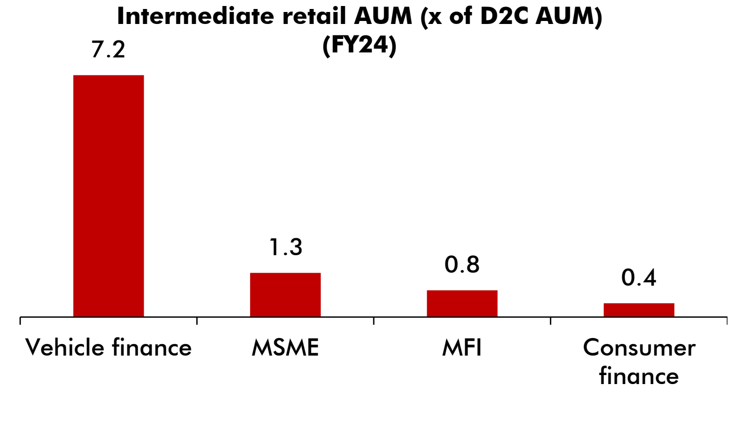
NACL's understanding of the end-user markets has helped it to lend to originator partners which on-lend in segments such as vehicle finance and affordable housing. Further, NACL's losses in intermediate lending are low at ~1% credit cost (1HFY26). Considering NACL's existing expertise in vehicle finance and affordable home loans, it can build out these product segments directly (through D2C), which would add to its scalability over the long term. For perspective, as of FY24, the intermediate retail portfolio was 7x of the D2C portfolio in the vehicle finance segment, implying AUM scalability and diversification potential. Further, in affordable housing where D2C portfolio is completely absent, NACL has lent ₹3.4bn through intermediate retail, indicating potential for adding a new segment for scale and diversification.

Exhibit 55: Intermediate retail lending in vehicle finance and affordable home loans indicates NACL has expertise in lending to these sector…



Source: Company, Ambit Capital research

Exhibit 56: …thus opening up room to pursue these product opportunities on the retail side as well, which could help in building scale profitably

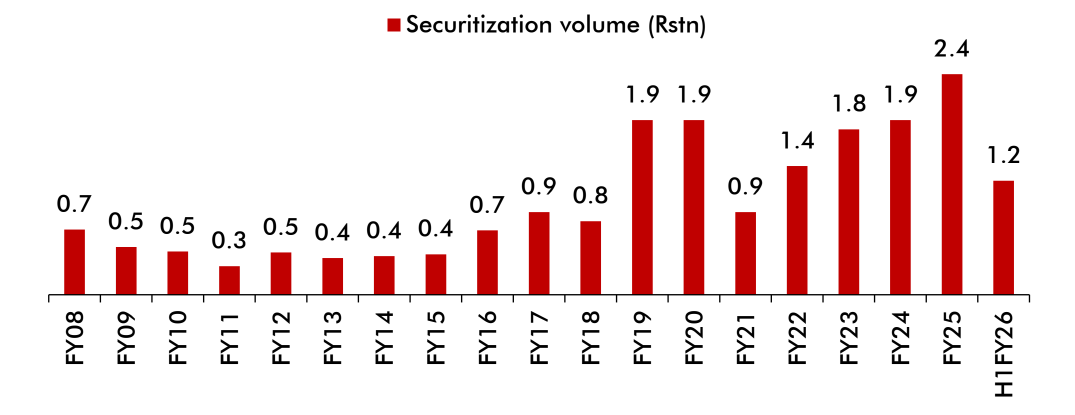


Source: Company, Ambit Capital research

Placement volumes to be aided by NBFC sector expansion; fund management growth to be led by emerging corporates

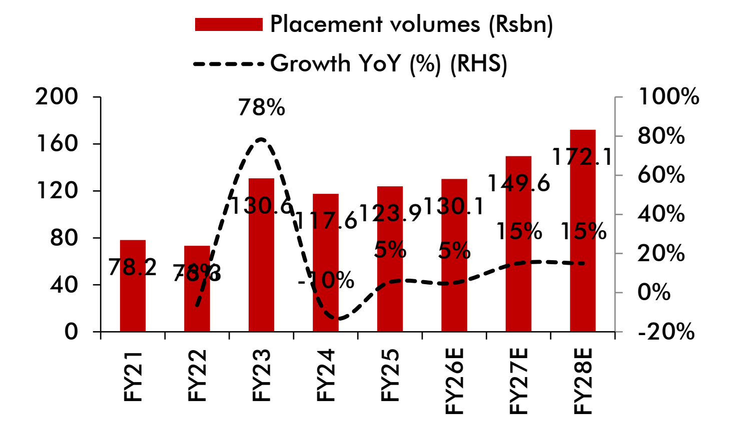
In addition to directly lending to other NBFCs (wholesale loans), NACL also facilitates funding from a broader investor base. Considering the expanding NBFC sector, we expect placement volumes to increase at 15% CAGR (FY27/28E).

Exhibit 57: Growing securitization volumes on the back of expanding NBFC sector and banks' requirements to meet PSL targets



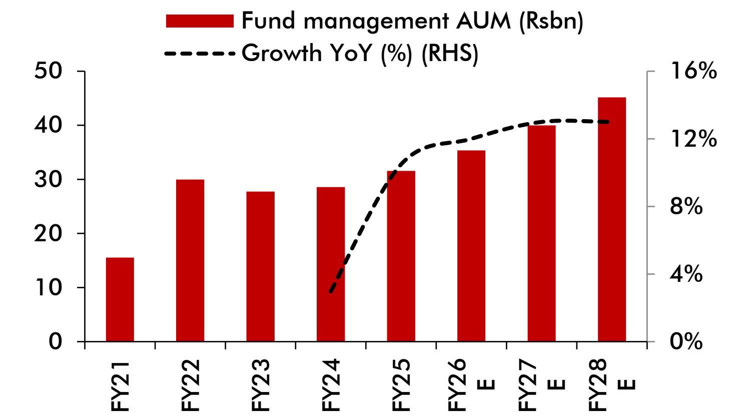
Source: CRISIL, Ambit Capital research

Exhibit 58: Growing securitization to aid placement volumes for NACL…



Source: Company, Ambit Capital research

Exhibit 59: …while emerging corporates' funding needs to aid fund management business



Source: Company, Ambit Capital research

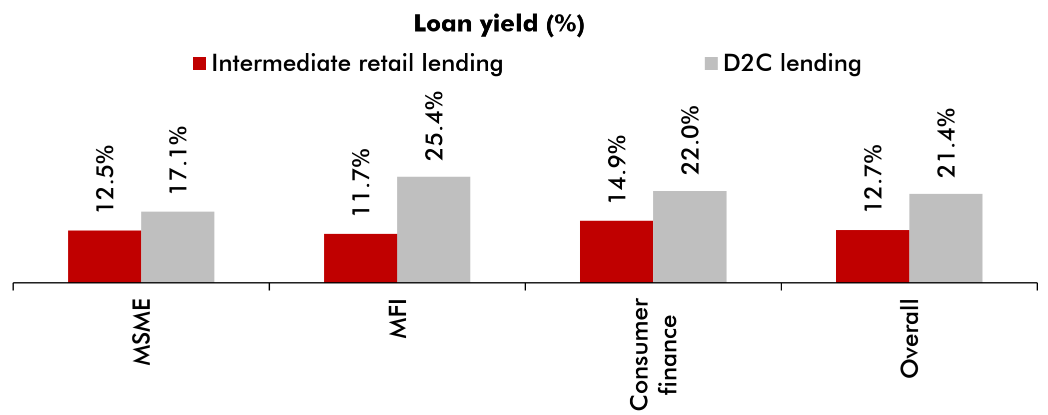
Retail-led NIM expansion cushioned by fee income

To improve capital allocation, NACL expanded D2C AUM mix to 52% in FY25 vs 19% in FY21, aiding 560bps NIM expansion. D2C spreads are 920bps higher than intermediate retail lending. D2C mix expansion to 64% by FY28E can drive further spread expansion of ~70bps. Hence, despite increasing leverage, we expect NIMs to be stable at 10.7-10.9%. In addition to interest income on lending, NACL boasts of a strong fee income engine as reflected in non-interest income at 36% of PBT vs 7-28% for peers. With placement volumes and fund management AUM increasing at 15% and 13% CAGR (FY27/28E), we expect fee income to increase at 15% CAGR (FY26-28E). Expanding NIMs and a strong fee income engine should provide NACL with a higher cushion to absorb credit losses vs peers.

Increasing D2C mix to aid lending margins

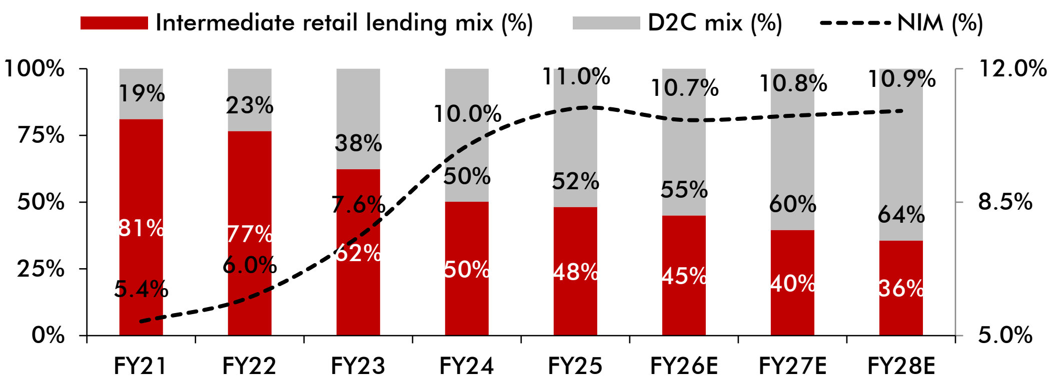
During FY19-21, NACL earned an average spread of 3.2%. This was largely due to a higher share of wholesale loans, classified as intermediate retail lending. For instance, in FY21, the share of intermediate lending in total lending AUM was 81%. However, management's strategy to focus more on the D2C segment (direct retail lending) augurs well from a spread/NIM expansion standpoint, given that yields are 920bps higher than those for intermediate lending. As of 1HFY26, the share of D2C lending has increased to 54% vs 19% in FY21. This has aided a 542bps expansion in NIM from 5.5% in FY19 to 11% in FY25. Given NACL's sub-scale operations, minuscule market share in overall MSME lending (₹32.5tn MSME credit) and expanding distribution, we expect D2C lending mix to increase further to 60%/64% by FY27/28E. This should lead to further spread expansion of 70bps by FY28E.

Exhibit 60: D2C retail lending is far more profitable than intermediate retail lending due to direct retail exposure



Source: Company, Ambit Capital research

Exhibit 61: Increasing D2C mix to aid stable-to-expanding NIMs and contribute towards ROA/ROE expansion

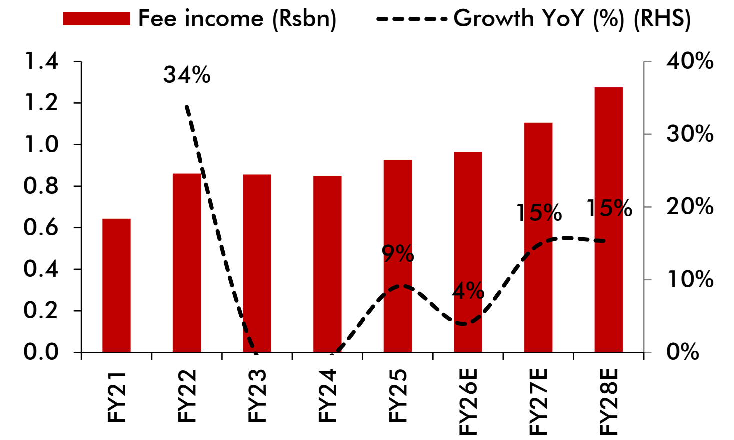


Source: Company, Ambit Capital research

Fee income complements overall revenues and provides cushion to credit costs

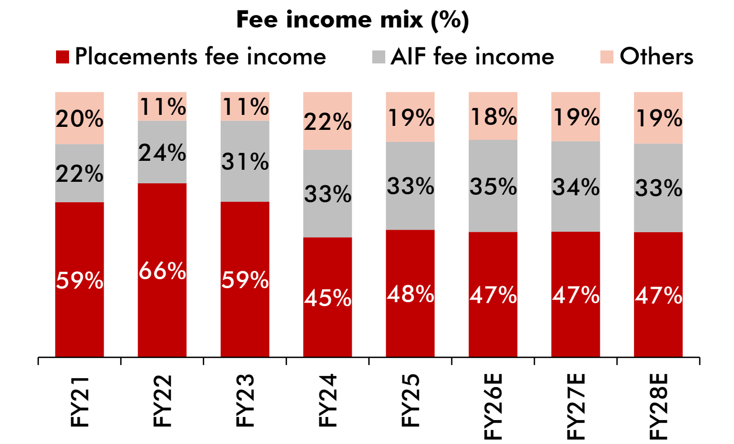
NACL enjoys a distinguished revenue stream, which is fee income from placement volumes and fund management. Amongst small/mid-size NBFCs, NACL's fee income/PBT ratio is higher at 24% (FY25). Having operated in placement and fund management businesses, NACL's long-vintage expertise and overall ecosystem approach should aid placement volume CAGR of 15% and fund management AUM CAGR of 13% over FY27/28E. Aggregate borrowings for a select group of small/mid-size NBFCs have grown at 22% CAGR over FY18-25. Against this, NACL's placement volumes have grown at 12% CAGR during the same period. We estimate 18% CAGR for borrowings by small/mid-size NBFCs, which should aid 15% placement fee income CAGR (FY26-28E). We are building 1% fund management fees and fund management AUM CAGR of 13% (FY27/28E), driving 10% CAGR in fund fees.

Exhibit 62: Fee income aided by growing placement volumes and fund management business...



Source: Company, Ambit Capital research

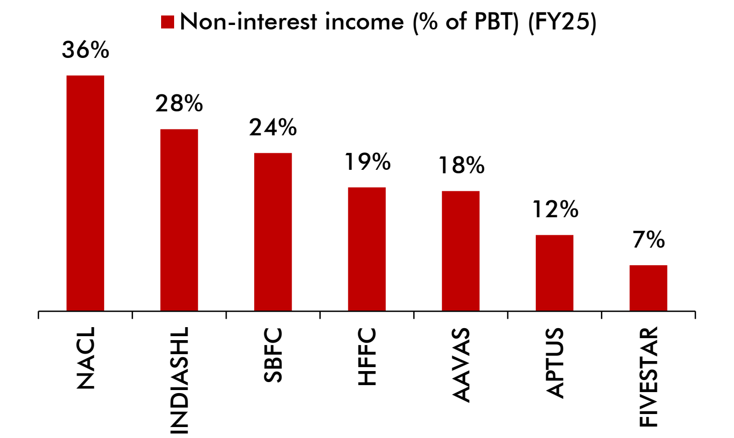
Exhibit 63: ...contributing to diversified non-interest income stream



Source: Company, Ambit Capital research

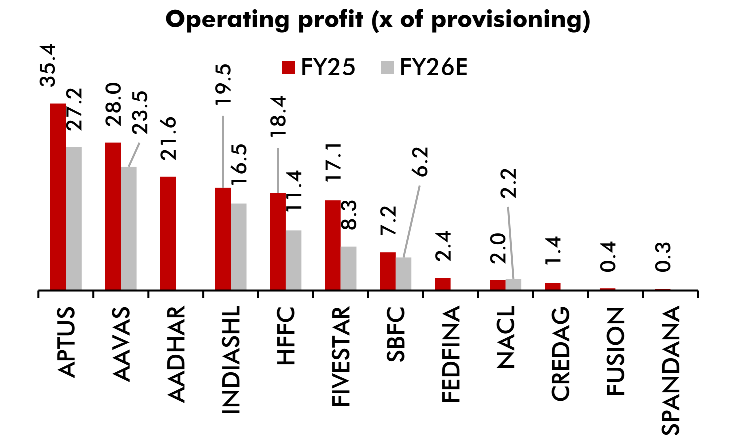
Even as lending spreads improve, non-interest income contribution to PBT would still be 24%, higher than small/mid-size NBFC peers. This provides a bigger cushion to NACL to take credit cost without impacting the ROE expansion trajectory. Even as we build for 2.6-2.7% credit cost (highest in our coverage), we expect ROE to touch 15.7% by FY28E.

Exhibit 64: Fee income from placements and fund management aid additional revenue lines...



Source: Companies, Ambit Capital research

Exhibit 65: ...strengthening operating profit to absorb credit losses from retail lending



Source: Companies, Ambit Capital research

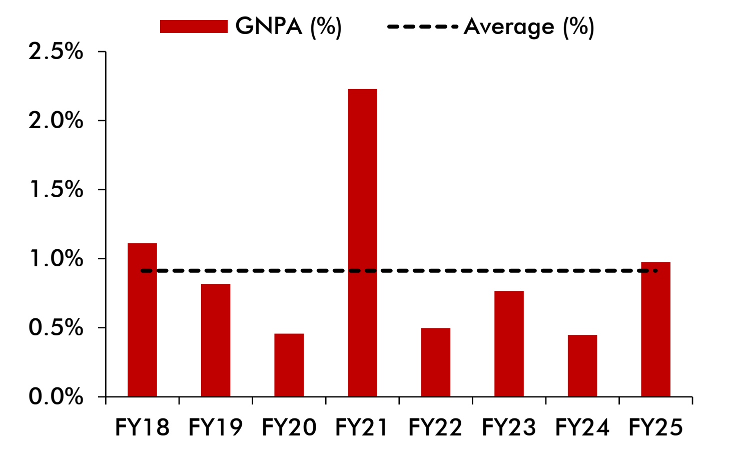
Turning cycle to aid asset quality improvement

Historically, NACL has demonstrated <1% GNPAs on average across the cycle (FY18-25) owing to a larger mix of intermediate retail lending, which is akin to wholesale lending. Besides this, NACL's security mechanism against default by the originator partner has also aided low NPAs. However, with increasing D2C mix (direct retail), we see structural credit costs rising to 2.6-2.7%, which is at par with the industry level for such exposures. That said, NACL is well equipped to absorb this given NIM expansion and strong fee income, which translates into 2.5x operating profit cover. We find comfort in NACL undertaking investments in product-specific collection and an underwriting team as it scales up D2C sub-segments. In the near-to-medium term, abating systemic concerns around MFI/MSME asset quality should aid credit cost reduction to 2.6% in FY27E vs 3.4%/2.9% in FY25/26E.

Higher focus on intermediate lending has kept NPAs low...

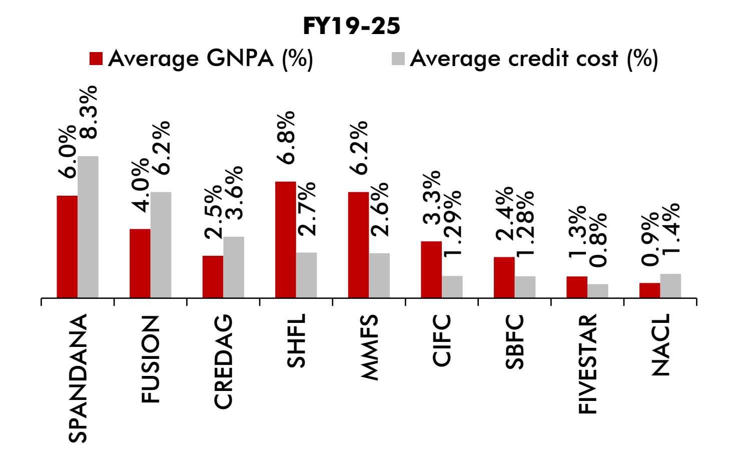
Over FY18-25, the gross stage 3 ratio has averaged 0.9%. At face value, these levels of stage 3 assets are lower than those of some MSMS-focused NBFCs, MFIs, and auto NBFCs. But NACL delivered these on the back of a higher intermediate lending mix (wholesale mix). This has helped keep average credit costs at 1.4%, including exceptional outcomes of 2.9%/3.4% in FY21/25. Checks indicate that, during underwriting of intermediate retail loans, NACL typically directs fund deployment (geography, customer type) rather than providing a plain-vanilla term loan, which can be deployed in any way. Further, NACL also provides security by creating a charge on the originator's receivables (110% cover or higher). Hence, as NACL scales up the intermediate lending piece at a more moderate pace (10% CAGR FY26-28E), risks of negative lumpy asset quality surprises appear low.

Exhibit 66: Average NPAs <1% over FY18-25 underscore reasonable underwriting, supported by higher wholesale mix



Source: Company, Ambit Capital research

Exhibit 67: Through-the-cycle credit costs are lower than other sub-scale NBFCs



Source: Companies, Ambit Capital research

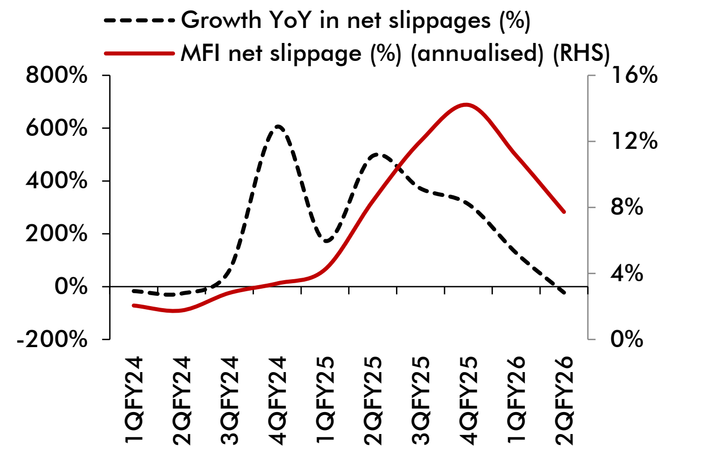
...investing in collections and underwriting for retail scale-up

D2C lending credit costs are 80-540bps higher than intermediate lending as NACL takes direct exposure/credit risk to underlying customers. That said, with increasing D2C business mix, NACL is simultaneously also investing in credit and collection infra, especially in the MSME segment. This augurs well from an asset quality standpoint. In case of merchant loans, NACL's bottom line is protected as it aims to generate 15-16% net yields after adjusting for 5% FLDG as well as through continuous refinement of pricing on a monthly basis. For instance, if the asset quality experience is deteriorating over and above the 5% FLDG, NACL typically increases the pricing of merchant loans to ensure 15-16% net yields.

Turning cycle to aid lower credit cost over the medium term; fee income cushion

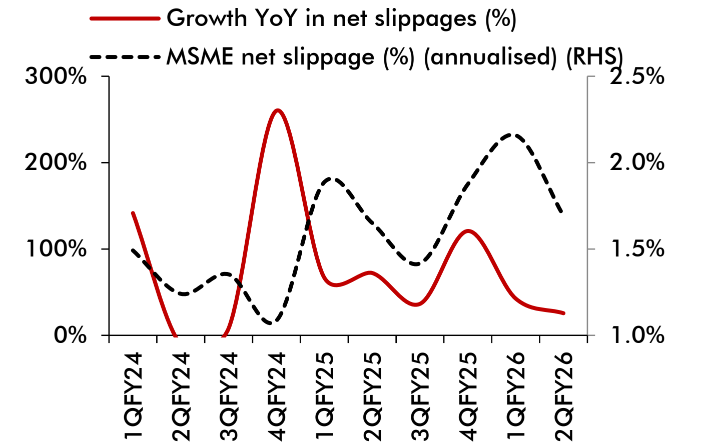
Overall, we expect NACL to deliver an average credit cost of 2.7% over FY26-28E. This would mainly be driven by a continuous shift towards D2C lending, which entails a higher steady-state credit cost run rate vs. the historical trend. In FY25, credit cost had a one-time impact of ₹680mn due to a change in FLDG accounting norms. Adjusting for this one-off impact, FY25 credit cost was at 2.7% vs 3.4% reported. Latest trends indicate systemic asset quality concerns are reducing, especially in MFI/unsecured lending. That said, small-ticket MSME loans remain a key monitorable.

Exhibit 68: Reducing over-leveraging concerns to aid MFI asset quality improvement…



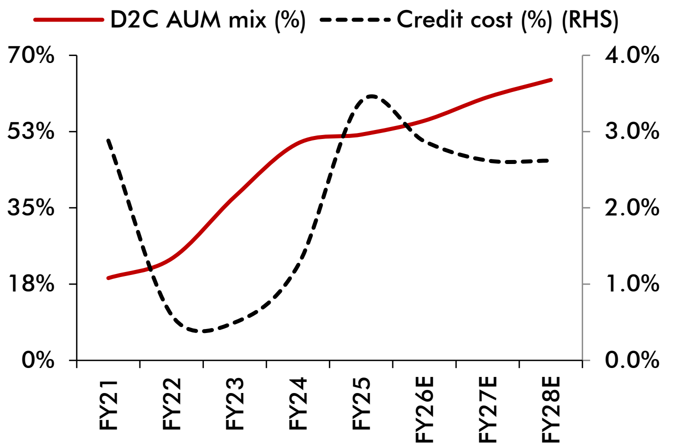
Source: Ambit Capital research, Ambit Capital estimates

Exhibit 69: …as well as improvement in MSME segment



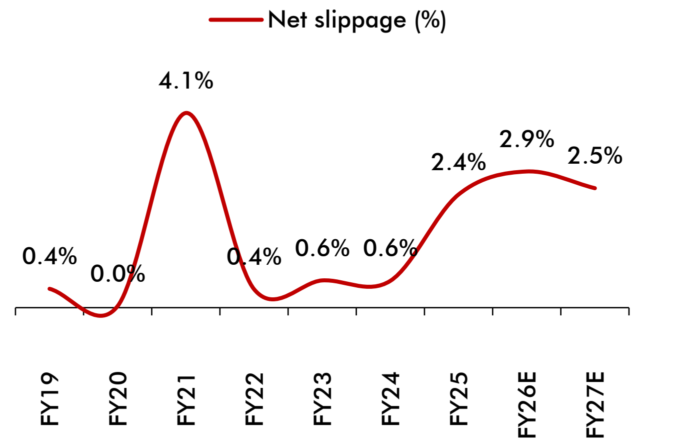
Source: Ambit Capital research, Ambit Capital estimates

Exhibit 70: Increasing D2C leads to higher structural credit costs but more than compensated for by higher yields



Source: Company, Ambit Capital research

Exhibit 71: Expect overall net slippages to reduce



Source: Company, Ambit Capital research

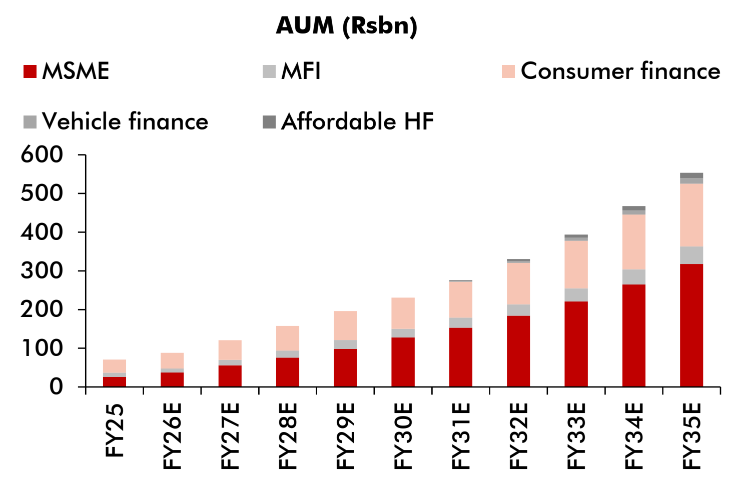
Valuation discount undermines recovery and structural improvement

NACL is underway with a structural transition from wholesale to retail-focused lender, as reflected in the D2C mix increasing from 19% in FY21 to 64% by FY28E. During this journey, we expect NIMs to improve by ~550bps, resulting in ROE expanding from ~5% (FY21) to 15.7% (FY28E) even after accounting for higher steady-state credit costs. Given AUM mix change and subsiding asset quality issues, we expect EPS CAGR of 41% (FY26-28E), higher than 16-25% for MSME-focused NBFCs/affordable HFCs. Underwriting expertise in vehicle and home finance provides option value, which could aid 23% AUM growth over FY25-35E, along with 15-16% ROE. But NACL's stock valuations at 50-60% discount to other sub-scale NBFCs seriously undermine improving prospects, likely due to legacy wholesale mix and MFI/MSME stress baggage. Our fair value factors 20% AUM CAGR/15% average ROE (FY26-36E), implying 1.2x/10x FY27E BVPS/EPS.

D2C shift enhances prospects + option value in vehicle and affordable mortgage financing

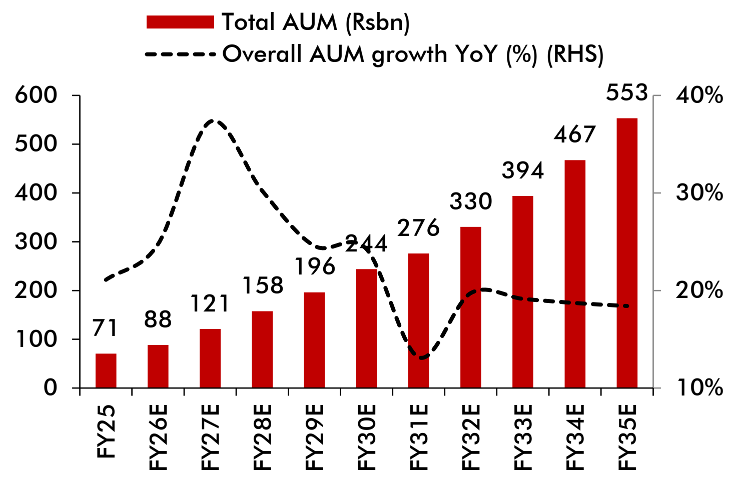
Historically, NACL's ROE was weighed down by a higher mix of intermediate retail lending, akin to wholesale lending, with low spreads (3-3.5%). However, increasing the D2C mix has enabled NACL to improve its NIM/operating profit margin, indicating an improving ROE profile. Over FY21-25, the share of D2C loans has increased to 52% and is expected to reach 64% by FY28E. In view of the continued D2C shift, we expect ROE to improve further to 15.7%/16.7% by FY28/29E, on the back of a 22% AUM CAGR (FY26-29E). In the long term, NACL has the potential to scale up retail/D2C vehicle finance and affordable home loan verticals, given that it has already built expertise in these segments through intermediate retail lending.

Exhibit 72: Building expertise in vehicle and affordable home finance through intermediate retail lending provides an option to scale up retail AUM in these segments...



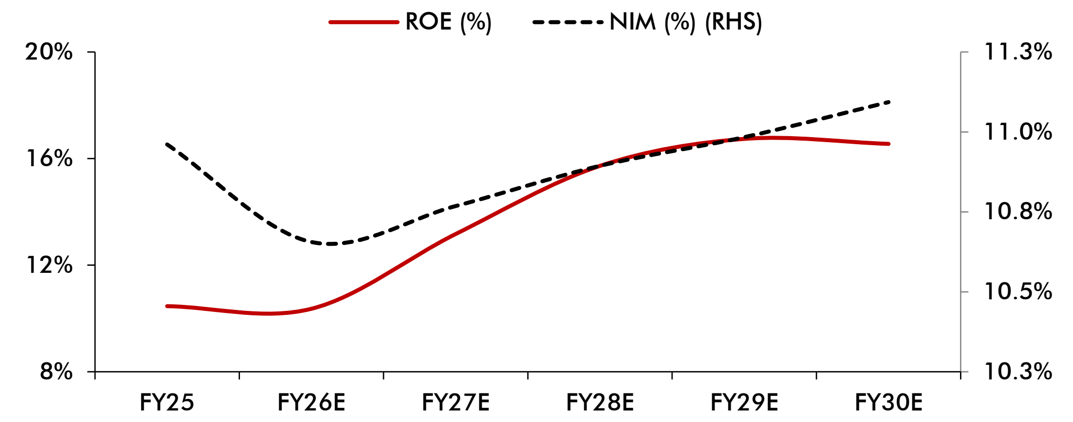
Source: Ambit Capital research, Ambit Capital estimates

Exhibit 73: ...which could aid long-term scalability...



Source: Ambit Capital research

Exhibit 74: ...as well as NIMs/ROE given these are value-accretive products vis-à-vis intermediate retail lending



Source: Company, Ambit Capital research

Medium-term earnings to be aided by cyclical recovery

In the medium term (FY26-28E), we expect earnings CAGR of 41%. This would be led by a reduction in credit costs as asset quality headwinds subside, especially in MSME/MFI segments (bottom-of-pyramid lending), and by NIM expansion driven by an increasing D2C mix. Over FY26-28E, we expect MSME-focused NBFCs to deliver higher earnings growth than affordable HFCs.

Exhibit 75: Expect AUM growth to rise, led by D2C mix, which would further aid NIMs. Reducing credit costs to further add to ROE expansion.

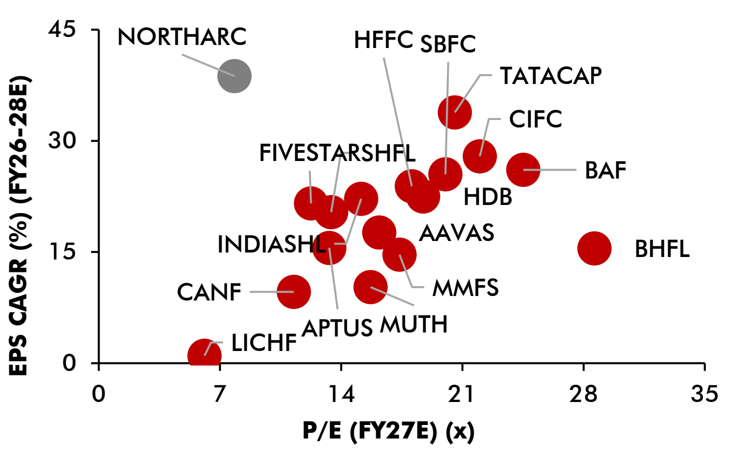
Key assumptions and estimates	FY23	FY24	FY25	FY26E	FY27E	FY28E	Comments
Key assumptions							
Lending AUM growth YoY (%)	27%	30%	16%	18%	25%	22%	Growth to recover in FY27/28E on the back of subsiding asset quality issues and small scale.
Intermediate retail lending (% of AUM)	62%	50%	48%	45%	40%	36%	
D2C lending (% of AUM)	38%	50%	52%	55%	60%	64%	Higher focus on direct retail lending to aid D2C mix.
Placement volumes growth YoY (%)	78%	-10%	5%	5%	15%	15%	Placement volumes to be driven by expanding NBFC sector.
AIF/fund management AUM growth YoY (%)	-7%	3%	10%	12%	13%	13%	Expanding emerging corporates to aid AIF growth.
NIM (%)	7.6%	10.0%	11.0%	10.7%	10.8%	10.9%	Increasing D2C mix to aid margin expansion.
Non-interest income (% of assets)	1.6%	1.4%	1.1%	1.1%	1.1%	1.0%	
Opex/assets (%)	4.5%	6.0%	5.8%	5.5%	5.2%	4.8%	Increasing scale to aid opex absorption.
Credit cost (%)	0.5%	1.2%	3.4%	2.9%	2.6%	2.6%	Credit costs to subside as asset quality headwinds subside.
Estimates							
Lending AUM (₹ bn)	90.1	117.1	136.3	160.2	200.3	244.8	
Placement volumes (₹ bn)	130.6	117.6	123.9	130.1	149.6	172.1	
AIF AUM (₹ bn)	27.8	28.6	31.6	35.4	40.0	45.2	
PAT (₹ bn)	2.4	3.2	3.0	3.8	5.4	7.4	
ROA (%)	2.8%	3.0%	2.4%	2.5%	2.9%	3.2%	
ROE (%)	12.4%	14.5%	10.5%	10.4%	13.2%	15.7%	ROE expansion led by increasing NIMs and reducing credit costs.
EPS (₹)	25.9	34.6	20.1	23.3	33.3	46.0	
BVPS (₹)	158.6	177.5	213.1	236.2	269.5	315.4	

Source: Company, Ambit Capital research

Deep discount to sub-scale NBFCs despite highest EPS CAGR

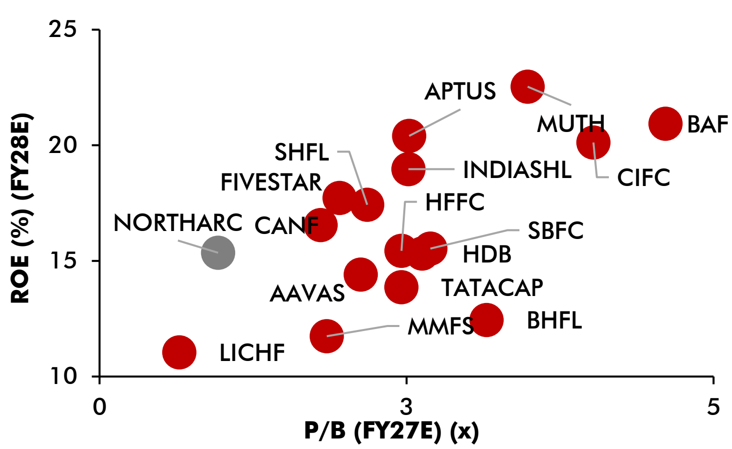
NACL currently trades at 1x/0.8x and ~8x/~6x FY27/28E BVPS and EPS, respectively. In comparison to other MSME-focused NBFCs (Five-Star, SBFC) and affordable HFCs, NACL's valuations are at a 50-60% discount despite offering a higher earnings CAGR. While medium-term earnings growth outperformance will be driven by turning the asset quality cycle, NACL's D2C shift strategy, along with non-interest income support from placement/fund management business, offers a play on a structurally improving business. In our overall framework for small/mid-size NBFCs, we prefer playing MSME-focused lenders like Five Star, SBFC and diversified players like Northern Arc over affordable HFCs given their diversification potential and ability to charge higher yields, enabling better scalability and higher ROE.

Exhibit 76: Earnings growth higher vs peers led by NIM improvement and credit cost reduction...



Source: Companies, Ambit Capital research

Exhibit 77: ...however, valuations undermine such recovery as reflected in 50-60% valuation discount



Source: Companies, Ambit Capital research

Ability to control credit cost volatility would entail higher ROE and more upside

In our base case estimates, we are building the cyclical impact of asset quality by assuming an increase in credit costs in FY29/30E to 3%. This is about 30bps higher than the peak credit cost (excl. one-time FLDG impact) of 2.7% in the current cycle. However, in a bull case scenario where NACL is able to reduce asset quality/credit cost cyclicity, structural ROE could be higher at 16%.

Exhibit 78: Bear/base/bull case scenarios

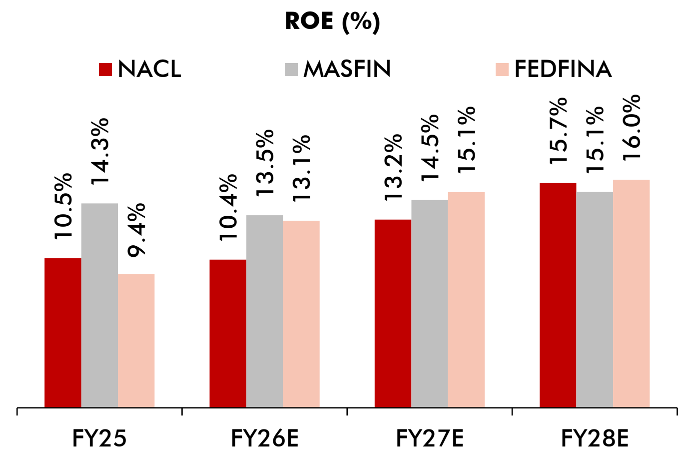
FY26-45E	Bear case	Base case	Bull case	Comments
AUM CAGR (%)	16.1%	18.1%	18.7%	
Credit cost (%)	3.0%	2.8%	2.5%	Bear case assumes higher asset quality volatility across cycles and hence higher credit costs. Bull case assumes that management will be able to reduce asset quality cyclicity.
ROA (%)	2.9%	3.1%	3.3%	
ROE (%)	14.0%	15.0%	15.9%	In bear case, higher credit cost should lead to lower ROA/ROE, while in the bull case, lower credit cost should aid increase in ROA/ROE.
Fair value est. (₹)	172	326	470	
Upside/(downside) (%)	-34%	25%	80%	
TP-implied P/B (x) (FY27E)	0.6	1.2	1.7	

Source: Company, Ambit Capital research

NACL offers higher EPS CAGR and ROE expansion vs MASFIN, FEDFINA

NACL's business model is similar to MASFIN. We also draw a comparison with FEDFINA given a similar MCAP and diversified AUM mix. Among these three names, NACL is better placed to deliver earnings growth and ROE expansion, led by the continued transition towards higher-margin D2C business and fee income support. Despite 41% EPS CAGR (FY26-28E) vs 21-28% for MASFIN/FEDFINA, NACL is trading at a 35% discount.

Exhibit 79: NACL to see higher ROE expansion/EPS CAGR led by increasing high-margin D2C mix...



Source: Visible Alpha, Ambit Capital research. Note: Consensus estimates for MASFIN, FEDFINA

Exhibit 80: ...but trades at lower valuation multiples

Company	EPS CAGR (%) (FY26-28E)	Trailing P/B (x)	Trailing P/E (x)
NACL	41%	1.1	14.3
FEDFINA	28%	1.9	21.3
MASFIN	21%	2.1	17.1

Source: Visible Alpha, Ambit Capital research. Note: Consensus estimates for MASFIN, FEDFINA

Exhibit 81: NBFCs financial summary

Companies	Bloomberg ticker	AUM growth (%)			RoE (%)			EPS (₹)			EPS CAGR (%) (FY26-28E)	BVPS CAGR (%) (FY26-28E)
		FY26E	FY27E	FY28E	FY26E	FY27E	FY28E	FY26E	FY27E	FY28E		
Auto NBFCs												
Chola Inv & Fin Co.	CIFC IN	19	18	18	18.6	20.0	20.1	59	79	96	28	21
Shriram Fin.	SFL IN	14	16	16	15.7	15.6	14.1	50	59	72	20	27
M&M Fin.	MMFS IN	12	12	12	11.1	11.1	11.7	18	20	23	15	8
HFCs												
LIC Housing Fin.	LICHF IN	7	7	7	13.4	11.2	11.0	94	87	96	1	11
Bajaj Housing Fin.	BAJAJHFL IN	21	23	21	11.8	11.7	12.4	3	3	4	15	13
Can Fin Homes	CANF IN	11	14	16	18.1	17.1	16.5	74	81	89	10	14
Aptus Value Hsg Fin.	APTUS IN	22	21	20	20.3	20.3	20.4	19	22	25	16	15
Aavas Fin.	AAVAS IN	17	17	16	13.8	14.1	14.4	82	96	113	18	15
Home First Fin. Co.	HOMEFIRS IN	25	23	21	15.5	14.5	15.4	51	64	78	24	14
India Shelter Hsg. Fin.	INDIASHL IN	29	27	23	17.3	17.9	19.0	47	56	70	22	17
Diversified NBFCs												
Bajaj Fin. (consolidated)	BAF IN	23	22	21	18.5	20.4	20.9	32	41	51	26	19
HDB Financial Services	HDB IN	13	15	17	13.9	15.0	15.3	31	40	47	22	14
Tata Capital	TATACAP IN	17	22	21	11.1	12.7	13.9	11	16	20	34	14
Northern Arc Capital	NORTHARC IN	18	25	22	10.4	13.2	15.7	23	33	46	41	16
Gold loan NBFCs												
Muthoot Fin.	MUTH IN	41	14	12	27.5	24.4	22.5	219	239	266	10	21
MSME-NBFCs												
Five-Star Business Fin.	FIVE-STAR IN	21	23	22	16.7	17.3	17.7	39	47	57	22	18
SBFC	SBFC IN	28	26	23	13.2	14.4	15.5	4	5	7	25	16

Source: Companies, Ambit Capital research

Exhibit 82: NBFCs valuation summary

Companies	Bloomberg ticker	TP (₹)	Rating	P/E (x)			P/B (x)		
				FY26E	FY27E	FY28E	FY26E	FY27E	FY28E
Auto NBFCs									
Chola Inv & Fin Co.	CIFC IN	1,436	SELL	29.1	21.7	17.8	4.8	4.0	3.3
Shriram Fin.	SFL IN	1,220	BUY	18.1	15.4	12.5	2.7	1.9	1.7
M&M Fin.	MMFS IN	249	SELL	19.5	17.0	14.8	2.0	1.8	1.7
HFCs									
LIC Housing Fin.	LICHF IN	578	SELL	5.9	6.3	5.8	0.7	0.7	0.6
Bajaj Housing Fin.	BAJAJHFL IN	88	SELL	35.3	31.9	26.5	4.0	3.5	3.1
Can Fin Homes	CANF IN	982	BUY	11.8	10.9	9.8	2.0	1.7	1.5
Aptus Value Hsg Fin.	APTUS IN	310	SELL	14.8	12.9	11.1	2.8	2.4	2.1
Aavas Fin.	AAVAS IN	1,509	SELL	19.9	17.0	14.4	2.6	2.2	1.9
Home First Fin. Co.	HOMEFIRS IN	923	SELL	23.5	18.7	15.3	2.9	2.5	2.2
India Shelter Hsg. Fin.	INDIASHL IN	1,118	BUY	19.1	15.9	12.8	3.1	2.6	2.2
Diversified NBFCs									
Bajaj Fin. (consolidated)	BAF IN	716	SELL	32.3	24.8	20.3	5.5	4.7	3.9
HDB Financial Services	HDB IN	870	BUY	23.9	18.7	16.0	3.0	2.6	2.3
Tata Capital	TATACAP IN	377	BUY	28.8	20.0	16.1	2.7	2.4	2.1
Northern Arc Capital	NORTHARC IN	364	BUY	11.2	7.8	5.7	1.1	1.0	0.8
Gold loan NBFCs									
Muthoot Fin.	MUTH IN	2,644	SELL	16.9	15.5	13.9	4.2	3.4	2.9
MSME-NBFCs									
Five-Star Business Fin.	FIVE-STAR IN	833	BUY	15.4	12.6	10.4	2.4	2.0	1.7
SBFC	SBFC IN	135	BUY	26.3	20.9	16.7	3.2	2.8	2.4

Source: Companies, Ambit Capital research

Risks and catalysts

Key catalysts

Spread expansion due to increasing D2C mix: Given management strategy on higher D2C contribution and revival in MSME/MFI segments, we expect spreads to expand 42bps YoY in FY27E, aiding NII growth.

Improving asset quality cycle to aid credit cost reduction: Given systemic improvement underway in MFI asset quality and MSME stress likely peaking out, we expect credit cost to reduce by ~25bps in YoY in FY27E.

Key risks

Key exposure segments remain vulnerable to downturn: NACL D2C operates in a customer segment that is highly vulnerable to economic downturns, given its low financial safety net. Unexpected economic shocks or downturns can impact D2C AUM growth and credit cost.

Increasing competition: In general, we have seen competition increase across retail financing sub-segments, including MFI, MSME and consumer finance. This could weigh on NACL's AUM growth and ability to sustain spreads.

Higher growth in intermediate retail lending can impact spread: Currently, we expect high-margin D2C AUM to grow at a higher rate. However, should the intermediate retail lending piece grow at a higher rate, as it is easily scalable, it would impact our spread/ROE expectations.

High state concentration: NACL's has relatively higher concentration in top-3/5 states. Any disruption in these states could pose execution challenges for NACL.

Exhibit 83: Explanation of our flags on the cover page

Segment	Score	Comments
Accounting	AMBER	Auditors noted audit trail gaps (as per FY25 annual report), which have been rectified. There are no revenue recognition issues.
Predictability	AMBER	FY25 profitability/RoE was adversely impacted by elevated credit costs amid the downcycle in the MFI industry.
Earnings momentum	AMBER	Currently, there is not enough coverage on the stock.

Source: Company, Ambit Capital research

Northern Arc (NORTHARC IN, BUY)

Valuation Methodology

We are valuing NACL based on excess ROE model. We are factoring 20% AUM CAGR and 15% average ROE over FY26-36E. We are assuming cost of equity of 14% and terminal growth rate of 5%.

Risks

Key risks to BUY call: (i) High exposure to vulnerable customer segment. (ii) Increasing competition. (iii) Higher growth in intermediate retail lending can impact spread expansion. (iv) State concentration can impact AUM growth and asset quality.

Financials – consolidated

Income statement

Particulars (₹ mn)	FY24	FY25	FY26E	FY27E	FY28E
Net interest income	**10,332**	**13,890**	**15,801**	**19,412**	**24,246**
Non-interest Income	1,465	1,384	1,634	2,002	2,400
Total Income	**11,796**	**15,274**	**17,435**	**21,413**	**26,645**
Total opex	6,360	7,344	8,361	9,707	11,143
Pre provision profit	**5,436**	**7,929**	**9,074**	**11,706**	**15,503**
Provisions	1,224	4,048	4,061	4,534	5,596
Profit before tax	**4,212**	**3,881**	**5,013**	**7,172**	**9,907**
Tax	1,025	848	1,253	1,793	2,477
Profit after tax	**3,177**	**3,013**	**3,760**	**5,379**	**7,430**

Source: Ambit Capital research, Company

Balance sheet

Particulars (₹ mn)	FY24	FY25	FY26E	FY27E	FY28E
Net worth	23,204	34,396	38,155	43,535	50,965
Borrowings	90,478	98,600	120,884	156,544	193,332
Total liabilities	**117,077**	**136,381**	**165,815**	**207,513**	**253,790**
Loans (on-book)	107,883	125,252	149,342	186,539	228,017
Cash & investments	4,077	6,474	8,462	10,958	13,533
Other assets	5,116	4,655	8,011	10,016	12,240
Total assets	**117,077**	**136,381**	**165,815**	**207,513**	**253,790**
AUM	**117,100**	**136,340**	**160,224**	**200,313**	**244,802**

Source: Ambit Capital research, Company

Key ratios

Particulars	FY24	FY25	FY26E	FY27E	FY28E
Lending AUM growth (%)	30	16	18	25	22
Placement volumes growth (%)	-10	5	5	15	15
Fund Management AUM growth (%)	3	10	12	13	13
EPS growth (%)	34.6	-14.4	16.2	43.0	38.1
Net interest margin (NIM) (%)	10.0	11.0	10.7	10.8	10.9
Cost to income (%)	53.9	48.1	48.0	45.3	41.8
Opex (% of AAUM)	6.1	5.8	5.6	5.4	5.0
Gross NPAs (%)	0.4	1.0	1.1	1.1	1.1
Credit costs (% of gross loans)	1.2	3.4	2.9	2.6	2.6
Provision Coverage (%)	82.4	61.0	52.0	52.0	52.0
Tier-1 (%)	18.1	23.5	21.4	19.5	18.7
CRAR (%)	18.3	24.7	22.7	20.8	19.9
Leverage (x)	4.8	4.4	4.2	4.6	4.9

Source: Ambit Capital research, Company

Valuation

Particulars	FY24	FY25	FY26E	FY27E	FY28E
BVPS (₹)	178	213	236	269	315
EPS (₹)	23.4	20.0	23.3	33.3	46.0
ROA (%)	3.0	2.4	2.5	2.9	3.2
ROE (%)	14.5	10.5	10.4	13.2	15.7
P/E (x)	11.2	13.0	11.2	7.8	5.7
P/B (x)	1.5	1.2	1.1	1.0	0.8
DPS (₹)	0.0	0.0	0.0	0.0	0.0

Source: Ambit Capital research, Company

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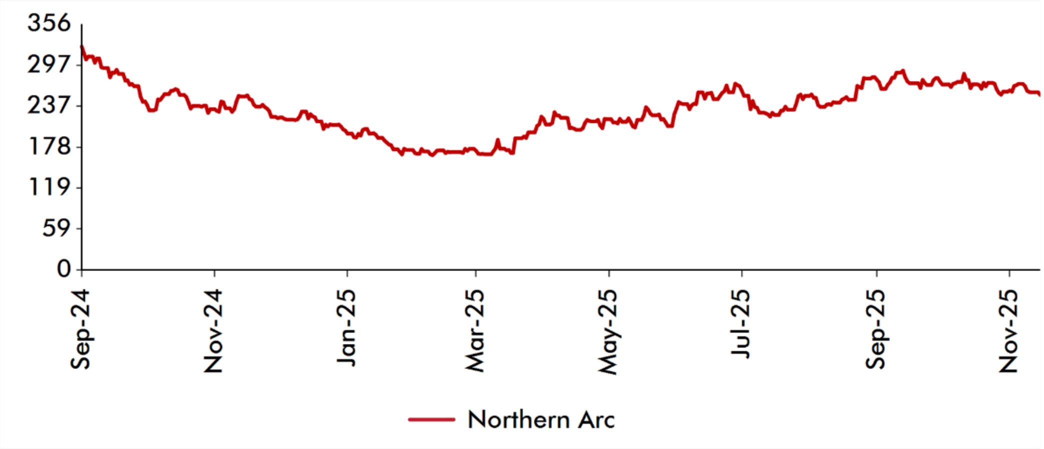
Northern Arc (NORTHARC IN, BUY)



Source: ICE, Ambit Capital research

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