

Northern Arc Capital Ltd. – Investment BUY Call – 6 Months Horizon

Dear Bajaj Capital Investors,

New Stock Recommendations for BUY on 10 May 2026

CMP -> 287

Upside Potential-> 15%

Investment Horizon -> 6 Months

Target price -> 330

Northern Arc Capital operates as a diversified retail-focused NBFC and structured credit platform catering to underserved credit segments across India. The company primarily works in the retail financial services and lending industry, with business exposure spanning MSME finance, consumer lending, rural finance, microfinance, structured credit, securitization and fund management. Over the last five years, the company has strategically transitioned from a largely wholesale and partnership-led lender into a higher-yielding Direct-to-Customer (D2C) retail-focused franchise. Management highlighted during the Q4FY26 concall that D2C contribution has increased significantly from 19% in FY21 to nearly 59% in FY26, which has materially strengthened profitability metrics and improved earnings quality.

The company operates through three major verticals — Direct Lending / On-book Lending, Co-lending & Structured Credit Solutions and Fund Management & Alternate Investment Platforms. Among these, the Direct Lending business remains the largest contributor to operating revenue, operating profit and PAT during FY26. This segment includes MSME finance, consumer finance, rural finance, LAP loans and digital retail lending products. Management indicated that the sharp improvement in business mix toward higher-yield retail assets resulted in a substantial expansion in NIMs from 5.6% in FY21 to 9.4% in FY26. The lending business continues to be the core profitability engine of the company, supported by robust growth in AUM, healthy spreads, improving operating leverage and declining credit costs.

Within the Direct Lending portfolio, Consumer Finance and MSME Finance emerged as key growth drivers during FY26. Consumer Finance AUM crossed INR 5,000 crore, with management highlighting that nearly 70% of customers are repeat borrowers, reflecting underwriting quality and strong customer retention. The company continues to target risk-adjusted yields of nearly 15% in this segment. Meanwhile, MSME Finance AUM reached INR 3,691 crore, registering strong 43% YoY growth, supported by branch expansion, secured LAP-based lending and improving collection efficiencies. Management emphasized that 100% of its MSME LAP portfolio is backed by registered mortgage structures, significantly strengthening collateral protection and reducing incremental credit risk.

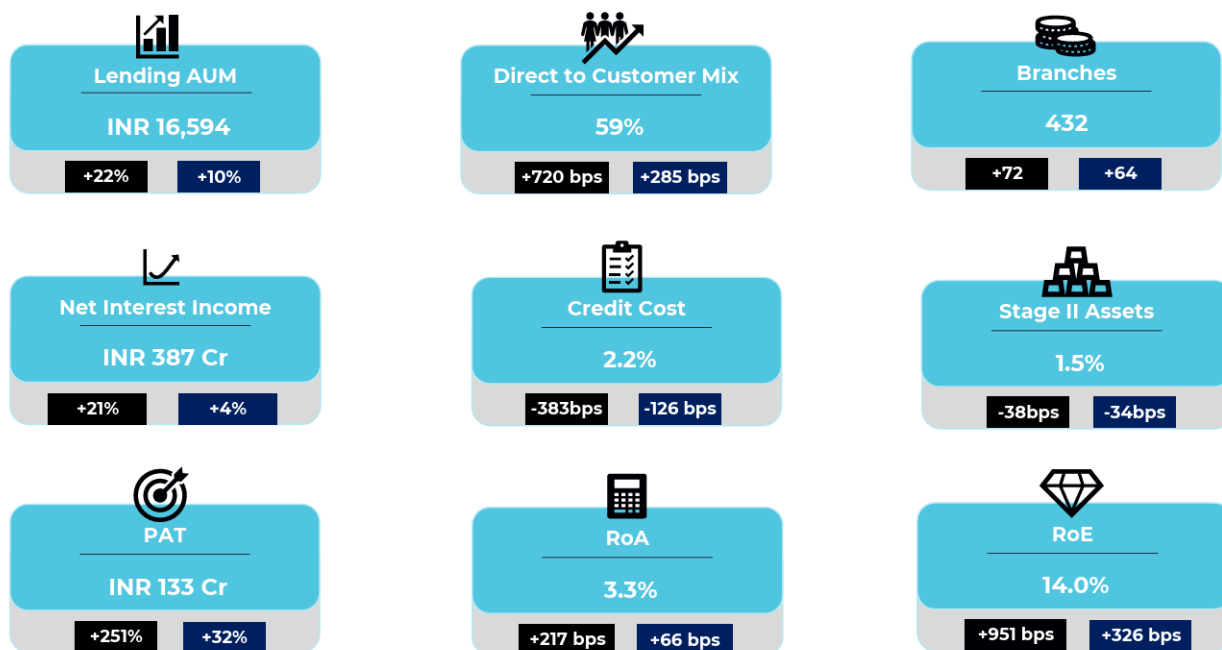
The company's Co-lending, Structured Credit, Placement and Securitization vertical represents its most scalable and capital-efficient business segment. Northern Arc has built a large ecosystem comprising 365 originating partners, with nearly 90% rated BBB and above. During FY26, the company facilitated placement volumes of approximately INR 11,800 crore while securitization volumes approached INR 10,000 crore. This vertical generates fee-based income through placement fees, loan syndication, securitization structures and co-lending partnerships with banks, NBFCs and financial institutions. Compared with on-book lending, this business carries materially lower balance-sheet risk and lower capital consumption while still generating attractive return ratios and stable fee income streams.

Among the company's three verticals, the Fund Management and Alternate Investment Platform business remains the highest-margin and least risky segment due to its asset-light operating model. The business manages nearly INR 3,000 crore of credit fund AUM and generated fee income of approximately INR 38 crore during FY26. Since this vertical largely earns management fees, structuring fees and distribution income rather than taking direct credit exposure, it inherently carries lower credit risk, lower provisioning requirements and superior operating margins. However, despite generating higher margins, its absolute contribution to PAT remains relatively smaller compared with the much larger Direct Lending franchise.

From a segmental profitability perspective, Direct Lending contributes the majority share of consolidated earnings, estimated at nearly 65–75% of operating revenue and PAT during FY26, while Co-lending & Structured Credit contributes approximately 20–30% through fee income, placements and securitization activities. The Fund Management and Platform business contributes a relatively smaller share of consolidated revenue, estimated at 5–10%, but delivers structurally superior margins due to lower operating and funding costs. Management commentary during the Q4FY26 concall clearly indicated that the company's strategic focus is gradually shifting toward a more diversified and capital-efficient financial ecosystem balancing higher-yield retail lending with scalable fee-income-led businesses.

Operationally, Northern Arc delivered a strong FY26 performance across key financial metrics. AUM increased 22% YoY to INR 16,594 crore, while FY26 NII rose 20% YoY to INR1,376 crore and PAT increased 33% YoY to INR 406 crore. Asset quality improved materially, with GNPA and NNPA declining to 1.2% and 0.6%, respectively, while credit costs moderated to 2.8% from 3.2% in FY25. ROA improved to 2.8% and Q4FY26 annualized ROA reached 3.3%, indicating improving profitability trajectory. Additionally, capital adequacy remained strong at 22.6%, leverage improved to 3.1x and management guided for sustainable 22–25% growth along with a medium-term aspiration of achieving mid-teen ROEs. Despite these improving operating fundamentals, the stock is currently trading at nearly 1.2x Price-to-Book Value, which appears inexpensive relative to its improving profitability profile, declining credit costs, expanding retail franchise and long-term scalable fee-based platform opportunities.

Q4FY26 Results:



■ YoY growth ■ QoQ growth

Q4FY26 & FY26 Operational Highlights:

INR crore	Q4FY25	Q3FY26	Q4FY26	YoY %	QoQ %	FY25	FY26	YoY %
Interest income ¹	519	602	632	22%	5%	1,969	2,279	16%
Interest expense	198	231	245	24%	6%	823	902	10%
Net Interest Income	320	370	387	21%	4%	1,147	1,377	20%
Fee & Other Income	30	31	27	-9%	-14%	102	108	6%
Net Revenue	350	402	414	18%	3%	1,248	1,484	19%
Employee Costs	68	85	85	25%	0%	285	331	16%
Operating Costs	52	53	59	13%	13%	171	198	16%
Total Operating Costs	121	138	145	20%	5%	455	529	16%
Pre-Provision Operating Profit (PPoP)	229	264	269	17%	2%	793	956	21%
Credit Costs	194	130	87	-55%	-33%	405	412	2%
Profit / (Loss) on Associates	0	1	(6)	-	-	(2)	(8)	-
Profit before tax	35	135	176	402%	30%	386	536	39%
Tax expense	-3	33	43	-	30%	85	132	56%
Profit after tax	38	102	133	246%	30%	301	404	34%
Profit after tax (excluding NCI)	38	101	133	251%	32%	305	406	33%

Happy investing!

Thank you and best regards,

On behalf of Bajaj Capital's Research Team