Paytm | Quarter Ended September 30, 2022 Results | Earnings Call

Date: November 08, 2022 **| Time:** 6 PM Indian Standard Time

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Moderator: Thank you for joining and a warm welcome to Paytm's earnings call to discuss its financial results for the quarter and half year ended September 30th, 2022. From Paytm's management team, we are today joined by Mr. Vijay Shekhar Sharma, Founder and CEO, Mr. Madhur Deora, President and Group CFO, Mr. Bhavesh Gupta, CEO Lending and Head of Payments, and Mr. Anuj Mittal, Vice President, Investor Relations. Before we start, a few standard announcements. This earnings call is meant for existing shareholders of Paytm, for potential investors and research analysts to discuss the company's financial results. This call is not for media personnel. If any media representatives are attending this call, request you to kindly drop off the call at this point. The information to be presented and discussed on this call should not be recorded, reproduced, or distributed in any manner. Some statements made on its earnings call may include forward looking statements. Actual events may differ materially from those anticipated in such forward looking statements. Finally, this earnings call is scheduled for 75 minutes. It'll have a presentation by the management followed by Q&A. Kindly utilize the Raise Hand feature of your Zoom dashboard if you're seeking to ask a question. We will unmute your line in the respective sequence and within the scheduled and permitted time. Please ensure your name is visible as first name, last name, followed by your company name at all times for us to identify you. The presentation, a replay of this earnings call and a transcript will be made available online subsequently. With this, I would like to request Mr. Vijay Shekhar Sharma to kindly initiate this earnings call.

Vijay Shekhar Sharma: Thank you and hello everyone. Good evening, good morning. I'm very happy to welcome you all for our earnings presentation for our quarter ending September, 2022. As you may have seen, we've had a good quarter as teams have performed very, very well on focusing our commitment to target EBITDA breakeven by the second quarter of next year, before ESOP cost, as you know. I will give you a little bit of a summary of the business model once again - we acquire customers, and we had 80 million transacting customers, and these customers in turn bring us merchants and we have 30 million merchants who in turn work and give commerce services to consumers. This makes our core business model to acquire customers on payments. And in turn, because this gives us insight, ability to distribute and a great brand name, we work with our lenders to distribute credit. So as you may be aware, over the period of time in the last four quarters, we have trimmed, since the IPO, a tremendous amount of businesses and focused on key business areas and pruned many business line items and made it very clean and clear that we acquire customers for payments and distribute loans from our credit partners.

In fact, our payments business is based on our merchant side business model, where we deploy QR codes and SSoundboxes or give them various devices for enterprise payments. We have expanded our offering to online and omni-channel merchants, which is an approach that the market is taking shape towards. I believe the payments business will become more and more omni-channel where online companies are going to be significantly offline, and offline companies are going to be online. Case in Point, Flipkart, with whom we work, has lots of online business. We also help them take offline payments because there is a lot of cash on delivery out there. So this is something we keep an attention to and then merchants use our platform, which we call consumer payments to collect payments so technically online merchants use our app to collect payments.

If you notice our payment business, which is our core business, is a model where we have added subscription and UPI MDR, which we don't account for yet in our business model till the time the government gives it; so subscription and merchant MDR revenues mostly, and little bit of platform fee. So these revenues right now that we're seeing on the right side are inclusive of MDR, subscription and select Customers platform fee only. We will book UPI subvention revenue only in the quarter that we get the money from the government. So these are the revenue line items that we ended up making for payment and enabling commerce and cloud service which also grew very healthily year-on-year. And as you can see, this is a business that is 55% up year-on-year, Rs. 1,550 crores. We believe the payment stack is a stack where we help merchants take payments in different avatars, locations, occasions and opportunities and enable them for commerce. This stack makes for a scalable, large, growing and profitable business model for payment and enabling cloud and commerce business.

Credit business, as you are aware, is founded on our abilities of digital lending, sourcing and cross-selling partnership with our lending partners and, over the period, helping them collect the loans. This makes this business model, as I call it, typically a funds management model where we get a fixed fee as well as a portfolio performance or carry, if you will. So you can imagine that this business model has an inherent compounding because when we disburse the loan, we get a certain percentage, but our ability of collecting, enables us to get sort of a portfolio performance bonus on that. An important thing to notice is that in the last quarter, RBI came out with clarification around digital lending, sourcing and EMI servicing collection opportunity, and Paytm's business model is clearly following the suggested guidelines. So we are very happy to tell you that we have been able to include every delta incremental, whether small or large, in the business model and the business model is very much aligned with how the regulator sees it. We continue to believe that this loan disbursement and collection business for India will play an important role in democratizing credit. If you remember, at one point in time, RBI leveraged public sector banks, then created private sector banks, then created NBFCs. Through this, different buckets of credit requirements were satisfied. Today, digital lenders, lending service providers or LSPs as RBI calls them, is what Paytm is here for - and it will generate and create new opportunities for disbursing digital credit. As you are aware, our digital disbursements are typically small ticket loans and we internally call these two businesses as 2 lakh rupee and two year tenure kind of loans where averages are 1 lakh plus one year and 150,000 plus one year and this is what the typical ticket size remains to be in personal loans and merchant loans. And for Paytm Postpaid, which is where customers get an overdraft limit from the lender to spend, it is typically now around Rs 4,500.

The good part in my opinion is that while these products have seen incredible year-on-year growth, they remain a very small fraction of our customer base, who are availing all three services for us and there is an incredible amount of headroom for our disbursement opportunity quarter-on-quarter and we continue to see reconfirmation from RBI that this business model and this workflow, which is how the regulator expects it, has now opened doors for many more lenders and many more partners to continue to join us and expand this business. I would now call upon my colleague Madhur to expand and give you a summary of overall business and the numbers. Madhur?

Madhur Deora: Thanks Vijay. Welcome everyone to our earnings call. I'm very proud to report that we had a very strong quarter. Our revenue growth as you've just seen from our earnings release, was 76% year-on-year. And our EBITDA before ESOP cost improved by 61% year-on-year. Just to get into that revenue from operations was Rs. 1,914 crores, so just under a billion dollar run rate. Our contribution profit continues to improve. It's 44% of revenue. A year ago this number was at 24% of revenue so a significant step change over the last 12 months, and even on a quarter-on-quarter basis, we have had a slight improvement and we're currently doing Rs. 843 crores of contribution profit. Our EBITDA before ESOP cost is really starting to see operating leverage come through, so Rs. 166 crores, less than 10% of revenue as a loss and there is nearly Rs. 260 crores improvement from a year ago at over a hundred crore improvement from last quarter. So by all measures, significant improvement in EBITDA performance for the last two quarters in a row. Operating highlights, Vijay already talked about, value of loans disbursed about Rs 7,300 cores up nearly six times and even on a quarter-on- quarter basis continues to grow at a very fast pace. And merchant subscription, which is our payment devices, primarily at 4.8 million devices, 3.5 million added in the last 12 months, and obviously faster right now.

This is our breakup of revenue. The basic point of this page is that we have seen platform expansion and increased monetization across businesses. So this is not one or two businesses carrying the overall performance. Our payment services business is up 56% year-on-year and up nearly 10%

quarter-on-quarter. Financial services obviously growing a lot faster, driven by lending. And commerce and cloud grew 55% YoY and 14% QoQ. Some of you may have noticed that there's a small amount of other operating revenue here. This has to do with basically a fund that RBI has which promotes the acquiring side for digital payment infrastructure and we are one of the beneficiaries of that. So it is payments revenue, but our auditors ask us to put that as other operating revenue rather than as payment services revenue. So that's where it is.

Our contribution profit like I said, a year ago was 24% of revenue. Now it's at 44% of revenue so both in absolute terms and even in percentage terms, significant increase. The two main reasons for this, the payments business for us, is now more profitable. You would've seen that our net payments margin has grown to Rs. 443 crores per quarter, there has been a significant improvement in that and we'll talk more about that a little bit later and clearly there is a benefit from high margin loan distribution giving us a better mix. On the right hand side, we're very proud of the fact that we continue to invest in our business in three main areas, technology, sales, and marketing. So for example, a year ago we had Rs. 94 crores of investments in our sales team or spends in our sales team every quarter. That number is now Rs. 172 crores. So despite increasing the investment which we believe is important for long-term scale and growth for Paytm, we are able to show operating leverage and go from 63% cost to 53% of revenue, so a significant improvement due to operating leverage. All of this translates into strong EBITDA performance. EBITDA losses have gone down by Rs. 260 crores due to huge operating leverage and our EBITDA margin has improved from negative 39% to negative 9%, so a 30% margin swing in a single year due to focused execution. And as you have figured out by now, 20% of that was from contribution margin improvement, and 10% of that was from reduction in direct expenses.

Just to get into the payments business a little bit, we as you know disclose both payment services to consumers and payment services to merchants, the growth of both these businesses was roughly the same, 55% year-on-year for consumer business. That is basically due to our growth of MTU and GMV. And on the merchant side, 56% growth which should do Rs. 624 crores. The reason for that was subscription and MDR revenue from offline merchants. We did see meaningful growth in revenue from online merchants this quarter as well, primarily because of some early festive in e-Commerce owing to big sales that happen in September and so on. As Vijay pointed out earlier, we don't have UPI incentives recorded this quarter consistent with our methodology last quarter. We only record UPI incentives when it is confirmed by MeitY. Net payment margin is up 5x year-on-year to Rs. 443 crores. And in addition to the revenue momentum, which is the main reason for it, we continue to focus on reduction in payment processing charges, and that's why we have got this significant uptake.

Some key operating metrics for payments, our MTU is up 39% year-on-year so a strong performance continues. This is driven by increasing customer acquisition at relatively benign CACs , but also an improvement in customer retention. Our GMV is up 63% year-on-year. Like we mentioned in the last quarter, our primary focus in our payments business is to have profitable revenue rather than GMV as a metric. So there's enough and more GMV that one can go out and get. The key thing is can you make revenue and you can make a net payment margin off of it. So that's what we optimize for. And as we had mentioned in the last quarter, we got rid of some business that we did not feel either generated revenue or net payment margins or had significant upsell opportunities. Despite that we are up 63% year-on-year. We'll continue to trim businesses that we feel don't make net payment margin, but we will continue to try to make our payments business more and more profitable. Merchant subscription, we have talked about that, we are now at 4.8 million. With that, I'll hand over to Bhavesh to take us through the next few slides please.

Bhavesh Gupta: Thank you Madhur. Hi good evening everyone, good morning. Our lending business continues to show good results. As you can see that we ended our revenue from financial services, the predominant part of the financial services revenue is coming from lending while our equity brokerage business and insurance businesses have also started to contribute. We had 4x growth from Rs. 89 crores last year at the same time. We ended at Rs. 349 crores and the important part here is that our entire focus continues to be on our lending business aligning to the new digital lending guidelines. We were always aligned. As Vijay said in his opening statement, we had to make some adjustments that we made to be absolutely aligned to those pieces and we are happy to inform you that there was no disruption in the business. Our business continues to perform every single day in the same manner and our BNPL business, personal loan business, and merchant loan business continues to demonstrate the strength of the opportunity that we will have through the platform.

Next slide, please. Coming to the numbers here, Postpaid, Personal Loans and Merchant Loans, the good information here is that all the three businesses are now showing tremendous growth. We are seeing Postpaid which moved up 5x, we actually disbursed Rs. 4,000 crores and if you look at the September run-rate basis, this business is obviously looking at a very healthy growth rate. It continues to demonstrate great penetration to merchants, and I'm very happy to inform you that we have now added 15 million merchants to accept Paytm Postpaid between offline and online. This is arguably the largest acceptance of any credit instrument across any funding sources in industry. And we do see a very large amount of merchants, both online and offline, coming towards getting to this 15 million addition and we hope to see this number continue towards the trajectory of 20 million and beyond in the next couple of quarters. On the fact that Postpaid is just still 4% of our MTU, that's the headroom that we see and we do see new acquisition happening continuously in a manner that we were seeing, let's say two quarters back. So there is no letdown of new customers getting on boarded on Paytm Postpaid and hence it gives us tremendous confidence that this growth of Paytm Postpaid will be as robust as we've seen in the previous quarters.

Coming to personal loans, I think personal loans have been growing very, very nicely on a small base but if I look at June 2022 and September 2022 from there also, it has almost doubled. There are two reasons behind this massive growth of personal loans. One, as the Paytm Postpaid business is maturing we are finding that our lenders are getting very comfortable seeing the mature book of the Paytm Postpaid business and offering them personal loans. So almost half of our personal loans have been disbursed to customers who have a running Paytm Postpaid loan with one of our lending partners so the journey and the entire customer appreciation of the product is extremely simple, and that's giving us a good growth trajectory and that is continuing because Paytm Postpaid is continuing. We will continue to see PL also continue off the back of Paytm Postpaid. The remaining 50% is the customers who are directly coming and applying for PL on a platform and we also see that trend actually being a nice trend because these are consumers who are looking for a bit of a higher ticket size amount, and they're seeking for something which is instant. And as you understand that 24x7, 365 days is the positioning of Paytm PL and that is giving us a good headroom and head start. We again don't see any issue with the TAM. Personal loans are less than 1% of our MTU and there is a fairly decent amount of headroom ahead for us while we are now almost averaging Rs. 900 crores plus per month on PL and we are clearly seeing good traction moving ahead for ourselves.

On merchant loans, there was a bit of a concern two quarters back when we were in COVID, how would merchants grow, et cetera. I think that's behind us now. The quarter behind June saw the first focus from our perspective, and lender's perspective in getting the risk capital back on merchant loans and this quarter was absolutely bang on. We saw great momentum, great acceptance from merchants in seeking our merchant credit on the back of great device growth that you've seen almost a million devices a quarter. This number is actually getting good traction and I can very clearly see that in the coming quarters merchant loans will continue to see great momentum on the back of our devices story. So all in all, overall disbursement business and even the collection performance that we will talk about in the further slides has been showing great momentum and we don't see this momentum getting slowed down. We do see calibration happen by our lending partners which is initiated by ourselves because we do understand that quality of portfolio for lending partners is a more important obligation than just getting the business. As a result of that, every month by design we work with our partners to take out the last cohort, 5% cohort in our businesses and make sure that that cohort is not getting renewals for the next month so that the portfolio quality is maintained the way it should be maintained so all loan is good story for us on the lending side.

This is the portfolio slide. This is a purely indicative slide as we always mentioned from a lending perspective for accumulation of all lending partners. As we are the collection outsourcing partners for our lenders this is an indication. There has been no change that we've seen over the last two quarters in this business. The bounce rates, the recovery rates in bucket one, the resolution rates on gross credit losses and the expected credit loss continues to be the way the lenders are expecting. I can also confirm while the ECL numbers called out, are the numbers that we've written, the actual credit loss performance is better than these numbers, but we continue to maintain a conservative stand and so do our lending partners in making sure that they are providing enough for the credit losses, looking at the macro headwinds or otherwise and hence the risk appetite and the risk portfolio is being built on this piece. So even on the portfolio we are seeing very good signals and we have not so far seeing any kind of macro headwinds that could impact the portfolio and that is giving strength to our lending partners and new lenders who come on board and expand this and entire business portfolio with Paytm.

Madhur Deora: Thank you Bhavesh. Just the last couple of slides, we want to cover commerce and cloud revenue. Our commerce business is up about 50% year-on-year. The travel merchants continue to do well. Our entertainment merchants typically have a seasonally weak quarter in Q2 both on movies and events side so that had some impact on our quarter-on-quarter performance. Cloud business, on the other hand, continues to do very well, 58% improvement year-on-year to Rs. 252 crores. We have started to see some early signs of recovery in advertising revenue. We did mention in the last quarter that there was a meaningful amount of pull back. So just towards the end of Q2 we started to see some recovery, but obviously it's too early to tell whether that'll continue for the next several quarters. On the other hand, we do see growth in our credit card distribution as well as on our PAI cloud revenue, so those businesses are doing well. And finally, we just wanted to summarize and leave this with you, our improvement in EBITDA before ESOP costs is continuing while continuing investments and scale and growth. So what we focus on is three main levers, one is platform expansion so that we have high monetization capacity down the road, our monetization engines working, which is revenue growth across all businesses, and finally on profitability, improving our unit economics while generating operating leverage as we continue to invest in our business and that is giving us improvement in EBITDA before ESOP cost. So that's all I had and I'll hand it back to the moderator who can help us with Q&A.

Moderator: Thank you Madhur. We will now proceed to Q&A. A reminder to utilize the Raise Hand feature on your Zoom dashboard if you seek to ask a question. We will unmute your line in the respective sequence. I request everyone to please have their company name next to their names. We do have a few common names so it will help us identify the right person. We'll just give a minute for the queue to settle in. We'll take the first question from Mr. Vijit Jain from Citi.

Vijit Jain: Hi thanks. I have a couple of questions. One on the personal loan side Q-o-Q has the growth come from outside of the Postpaid base of customers? I ask that because I recall last quarter the share of Postpaid customers was 50%. This quarter it’s 40%. I'm just wondering if there's greater growth from outside that base, that's one and I'll just come back with the next question.

Bhavesh Gupta: Sure thank you Vijit for the question. So your observation is right. Actually it is because we have grown much, much larger than the previous quarter. The percentage will look like that 40% has come from Postpaid, but there's no material change. One definite material change which has happened is that as the personal loan book has started to mature more and I mentioned about this last quarter also, earlier broadly we were doing about 10% to existing personal loan customers when they close their loan a new loan by the lenders, that percentage has now started to inch more towards 15-17%. And the ticket size is a bit larger so hence the value of loans coming from existing personal loan customers has increased, but the Postpaid number of loan penetration to overall PL has remained the same. So it's more of a mathematical outcome, but no material change in terms of the customer adoption of the product.

Vidit Jain: Got it. Thanks Bhavesh. My next question is in terms of overall lending partners. Is that number at 8 right now, same as last quarter and could you share what percentage of loans disbursed is disbursed by the partner with the highest share among those 8?

Bhavesh Gupta: Yeah, so the number is actually nine. We've got three card partners and we have got I think about five or six lending partners. We don't actually disclose the share that we do, but I can definitely mention to you that we have partners across this category who do personal loans, Postpaid and merchant credit so there is no one partner who's taking the lion’s share of this business. There is a material distribution basis the lender's appetite on how much business they want to take, but currently it is reasonably well distributed amongst the partners that we have. And to your other question, we had announced publicly that we've added one more lender which is Piramal Enterprises. Hopefully we will take them live sometime in quarter 4 and we have a decent pipeline of new lending partners that intend to get onboarded to leverage the Paytm ecosystem and the platform for credit and we obviously welcome all the new partners coming on board and we will be adding them in the course of time.

Vijit Jain): Great. Thank you Bhavesh. Those were all the questions. I'll jump back into the queue.

Moderator: Thank you Vijit. The next question we'll take from is Mr. Saurabh Kumar from JP Morgan. Saurabh, your line is unmuted.

Saurabh Kumar: Yeah. Hi, I'm Audible?

Moderator: Yeah, you are.

Saurabh Kumar: Okay, just three questions from my side. One is the indirect cost reduction which we've had, or at least, I mean, the cost control we have. How should we think about the indirect cost growth from here on? The second is, if we look at the EBITDA trend, it's very clear that you could turn positive or EBITDA neutral by at least maybe the March quarter so will that be a fair assumption to be making? And lastly, on the credit card business could you just comment on what's the card sourcing velocity at this point of time and how should we think about it? Thank you.

Madhur Deora: Thanks Saurabh. Maybe I'll take the first two and Bhavesh will take the third question. So on our indirect expenses and EBITDA, maybe I'll take it together, so we have given EBITDA guidance for breakeven which is September 2023 quarter. Compared to the time when we gave that guidance, we are ahead of our plans, but we would like to maintain our September 2023 guidance for EBITDA breakeven. On indirect expenses in particular, obviously our focus is to make sure we reduce our EBITDA losses as per the guidance that we have given, but when we do see opportunities, and we do see many opportunities to invest in our business for short and medium term growth we do take those opportunities. While our last quarter number was relatively flat on indirect expenses, you would've seen that on a year-on-year basis, we've actually increased our indirect expenses by 47%. So we do continue to make investments in our business and we have the sort of luxury of being able to do that because our revenue and contribution margin are performing really, really well. So we can achieve both objectives of reducing our EBITDA while continuing to invest in indirect expenses where we see high ROI. Bhavesh you want to take the question?

Bhavesh Gupta: Yeah, sure. Yeah Hi Saurabh. So Saurabh on the Cards business we are very excited in building the cards business. It's a very nascent business that we started about 18 months back. We are very privileged to have two of India's largest issuers as our partners, HDFC Bank and SBI Cards, and hence our portfolio of cards business has shown robust growth. While we've not declared actual numbers, but I can only suggest to you that at this point in time that business is operating much beyond our expectations in terms of customer adoption coming on the back of the fact that the customer value proposition, which is powered by our issuing partners and obviously powered by Paytm platform usage is really getting us good customer quality which our issuers are very happy with, and we are seeing very high scale of the card business. What we believe is our aspiration to build at least a million cards a year on the issuing side, maybe over the next 12 to 18 months continues to remain as strong as ever. And we would be guided by that as we build this cards business and hopefully in the future as we feel that is now a material side of our business, we would like to disclose more details about it.

Saurabh Kumar: Oh, so thank you. So just 1 million cards in 12 months is that right?

Bhavesh Gupta: No, I'm saying we continue to aspire to build a million cards originating over the next 12 to 18 months and that's an aspiration that we would like to see happening .

Saurabh Kumar: Okay got it, thank you.

Moderator: Thanks Saurabh. The next question we'll take from is Mr. Kunal Shah from ICICI. Kunal you can unmute your line.

Kunal Shah: Hello? Yeah, am I audible?

Madhur Deora: Yeah Kunal, you're good.

Kunal Shah: Yeah so firstly, again, to touch upon this question with respect to the Postpaid, in fact when we look at the overall traction in terms of the number of loans disbursed in fact normally it used to be the run rate of say two odd million, but this quarter it seems to be slightly on a lower side. So I just want to get a sense in terms of Postpaid, why it's just like 0.6 odd million and how should we look at it because it's hardly like 7-8% kind of a sequential growth?

Bhavesh Gupta: Yeah so Kunal we had to make some adjustments with regard to new digital guidelines which we had called out very clearly, which meant that our lending partners and ourselves had to make adjustments in terms of fund flow. That clarification took time from the regulator. I think it came in about 40, 50 days later on, that the entire fund flow has to be reorganized in a manner, which was the way we were doing it and hence that is a disruption that we saw in the last quarter but from a new customer origination and acquisition perspective, we continue to see very robust growth. Every month we're onboarding more than 400,000 new Postpaid customers so that hasn't stopped. It was just a recalibration that we had called out in a specific call that we had made to align to the fund flow , which took some time for us to align and clarify, which is now behind us.

Kunal Shah: Okay so when we look at it now incrementally the run rate should get back to that number and this was just a quarter’s disruption and that's more or less I think…

Bhavesh Gupta: Yeah, so very honestly we don't track this on this basis that how much is Postpaid doing in terms of number of new incremental loans. We track on the basis of new customer acquisition. I can definitely confirm to you that new customer acquisition on Postpaid will be the highest ever that we've seen thus far, and will continue to have the same trajectory. What that will mean in terms of new customers converting their Postpaid lines to actual loans is a matter of conjecture, which will happen as per the customer’s expectation in the next quarter. It should broadly be in the same range, but I can't comment that it will be 2 million or one and a half million or two and half million, but it'll be in that range for sure.

Kunal Shah: Sure and secondly with respect to the direct cost on the promotional cash back and incentives, whatever incremental is there for the quarter, maybe almost like more than 30% kind of sequential rise, any colour that you can share in terms of how much would be related to the payments and how much would be towards the rolling out of the financial services or maybe enrolling more of the customers for that service and how much would be towards the commerce?

Bhavesh Gupta: Yeah so actually the cash back is put predominantly, into two parts, which is that we do cash back on our payment services. There are some customer incentives that we also used to pass till September for promoting Postpaid at different online merchants on behalf of vendors. So that cashback increased because Postpaid GMV was very high in the last quarter. That cashback saw a rise, but what we figured out very clearly now with our partners, that is actually a payment charge, so from next quarter onward that will start showing in our payment charges. So that Postpaid incentive will all move to payment charges. So predominantly the increase that you've seen in the last quarter is driven by Postpaid.

Kunal Shah: It's driven by postpaid, yeah.

Bhavesh Gupta: Postpaid.

Vijay Shekhar Sharma: Kunal, one more thing I'd like to add here. Your question was look at cashbacks in let's say payments, commerce and financial services so Postpaid because we are accounting for as a payment, so it'll go towards payment charges from next quarter but the commerce part, incidentally, we internally have a key KPI that it should not be more cashback than the margin. We've talked about in our previous earnings also where our commerce business continues to operate with profitability as a target and it has achieved profitability, complete operating full cost loaded profitability. And like you said, I mean we don't have it immediately available that this much was for payment this much for commerce, in payment the cashbacks are given only as an incentive to the new customer. If you are a first time customer, we give you incentive to try out different services, but if you are an old customer, that is reduced dramatically and that is how the cash back and marketing expenses were reduced over the period.

Kunal Shah: Sure and lastly in terms of the commerce now that maybe with the opening up of all the activity levels and the situation stabilizing and now we would get more sense in terms of how the overall positioning is say for Paytm in the commerce so sequentially I think that was a dip, but otherwise how should we actually see the traction with respect to the commerce business going forward?

Vijay Shekhar Sharma: We do three kinds of commerce. One is led by shopkeepers' commerce - deals, gift vouchers that shopkeepers enable. Second is ticketing commerce which is led by movie, train, cinema and all these. The movie part has not come back by the way. Movies' footfalls have not recovered yet which is one of the important drivers of the commerce business. Third is advertising, which is definitely not just because we treat credit cards as advertising so for us it definitely has grown. And like I said, the first part where the help to shopkeepers has grown and travel has grown, but not movies.

Kunal Shah: Yeah, yeah. Thanks. Thanks and all the best .

Moderator: Thanks Kunal. The next question will be from Manish Shukla from Axis Capital.

Manish Shukla: Good evening and thank you for the opportunity. Firstly, what does it take for a merchant to start accepting BNPL because that number is growing very fast, currently at 15 million merchants. So what does a merchant need to do to start accepting BNPL?

Bhavesh Gupta: So Manish the merchant has something called Paytm for Business app. On the Paytm for Business app, the merchant can subscribe to the service. Depending upon the category of the merchant there is a charge the merchant has to accept and it could also be given free if you are a very small merchant, and we would like to enable that merchant for Paytm Postpaid. The moment the merchant accepts terms and conditions of Paytm for Business app, the merchant is onboarded. If the merchant meets the risk criteria as defined by our risk team because it's a credit instrument, the merchant is allowed to go through risk criteria. So that is how the entire onboarding process works. It's complete digital and it's obviously DIY for the merchant.

Manish Shukla: So the number of devices we have is at 5 million and acceptance of BNPL is at 15 million. Should we think of that 15 million as a potential universe where you can cross sell devices?

Bhavesh Gupta: Yeah I think that could be one of the ways because these are materially decent size merchants then only they meet the risk filter and also they meet the classification for themselves to accept a credit instrument. So you could say that could be an opportunity, but not an exact opportunity, but that could be an opportunity for us.

Manish Shukla: Okay moving on to platform fees, could you tell us how does a platform fee works and what percentage of your users might be paying platform fee at the moment?

Bhavesh Gupta: See platform fee as a part of our revenue is a small number. We for our previous categories when customer come on the Paytm app, for doing certain set of transactions and activities, let's say movie ticket booking or doing some recharges etc, there is a small fee which is levied on the cohort of customers because we offer them various other value added services, including and not limited to things like bill reminders, auto pay etc. And hence these customers subscribe to these services and they end up paying a platform fee. But purely from a rupee quantum of this charge, that charge is still very immaterial to the overall revenue that we make from payments.

Manish Shukla: And has there been any communication or otherwise from either the regulator or government about this platform fees being levied because in some sense technically that makes UPI as not a free service, right?

Bhavesh Gupta: No so I just want to clarify Manish there are two different parts. There is no platform fee that we are charging to merchants when we are giving them any kind of funding source. Some of the competitors do that in the online space. We are not charging those kinds of fees, etc. This is the fees that a consumer is paying when they're trying to consume certain services on the Paytm platform. The regulator has very clearly called out on what services you can charge and on what services you cannot charge. So once they've allowed us to charge, we are charging on them. So it is completely compliant to the regulatory guidelines.

Manish Shukla: Okay thanks and the next question, in response to an earlier question you said that starting next quarter the accounting will move from cashback to processing charges. Is it material enough for it to read to a sequential decline in net payment margins?

Bhavesh Gupta: Madhur, would you take that?

Madhur Deora: Yeah, it is a material number, but our net payment margin sort of continues to grow so it'll have some impact, but we don't think it'll lead to a drop in that payment margin per se.

Manish Shukla: Okay the last question is there any update on your payment aggregator application with the Reserve Bank?

Bhavesh Gupta: Yeah so the payment aggregation which is our Paytm payment services license is in progress. Whatever engagement that we had to do with RBI has happened. As you can see publicly, various other PAs have started to get the license. We do believe that we should also be getting our own license in the due course of time and fairly soon.

Manish Shukla: Okay sure. Those were my questions, thank you.

Moderator: Thanks Manish. The next question we will take from Rahul Bhangadia from Lucky Investments.

Rahul Bhangadia: Yeah thank you for taking my question sir. Congratulations on a great set of numbers. Just one question: what should we expect the CapEx rate to be on a run rate basis? I saw H2 last year and H1 this year were reasonably higher than what we used to see before.

Madhur Deora: Yeah so Rahul most of our CapEx is related to Soundbox and devices and as you know we have ramped that up and we have continued to talk about there being a large opportunity there. So currently I think we're doing somewhere between Rs. 120 to Rs. 150 crores a quarter. Our overall CapEx as I said, vast majority of that is related to devices and you should expect that to be broadly the level over the next few quarters.

Rahul Bhangadia: So roughly what four to five hundred crores per annum is the CapEx we should expect?

Madhur Deora: Yeah, I said 120 to 150 a quarter, five to six hundred crores a year.

Rahul Bhangadia: Yeah and the related question would be what would be the depreciation policy here because now we are running a run rate of about Rs. 400 crores of depreciation per annum and we're doing a CapEX of Rs. 500 crores or maybe Rs. 600 crores. What's the policy that we are looking at here?

Madhur Deora: Yeah the philosophy that we took on depreciation is that we wanted the depreciation rate to be faster than the average life of a device. So for Soundbox we depreciate it in two years, for card machines we depreciate it in three years, which we think is at least 20% to 30%, if not more, less than the average life of the device. And the way we price this is a payback period, which is better than the depreciation period for the device. So we try to be conservative on each one of these things, but to answer your direct question, Soundboxes are for two years and card machines are for three years.

Rahul Bhagadia: Thanks Madhur, thank you so much.

Madhur Deora: Thanks Rahul.

Moderator: The next question we'll take from Mr. Sameer Bhise from JM Financial.

Sameer Bhise: Yeah hi thanks for the opportunity. Can you talk a bit about the GMV per MTU metric? I think the last couple of quarters probably we have not alluded to , but how do you think about it over the medium to long term?

Madhur Deora: Just to be clear, the reason why we don't refer to that number is because effectively we have a total GMV number which is all transactions which are processed by Paytm and in some of those cases that is being done by the MTU numbers that you see, but in some cases, that is actually not being done by that MTU number. So for example if I have a card machine at a retail shop or at a petrol pump, they might be accepting credit cards, which does not belong to our MTU. And the same thing would happen in the online world, same thing would also happen when somebody uses a third party app to scan a Paytm QR. So there's a fair amount of GMV in our business which is unrelated to the MTU base that you see. So taking the GMV divided by MTU is probably not taking apples to oranges and as a result we don't calculate that and get that number because it may be misleading to think that it is this MTU which is generating that GMV. Does that make sense, Sameer?

Sameer Bhise: Yeah, probably I'll take it offline as well. Secondly, there's a news article on RBI giving some clarifications or responses on the IT audit. It would be helpful if you could give us some sense on that.

Madhur Deora: So we actually have in our earnings release given a statement on this. So I'll just refer you to that. In summary the Paytm Payment Bank management has told us that they have received the IT audit report and RBI's observation on the report. As per the preliminary assessment done by them most of the observations are around continuous strengthening of IT processes, IT outsourcing processes and operational risk management. And the bank is in the process of responding to the RBI and they're just obviously very highly focused and prioritizing the conversation with the RBI to make sure that they're fully compliant in letter and spirit. So that's sort of the update that we have and obviously if we have more updates we'll share them with the stock exchanges, but I'll just refer you to the note that we have in the earnings release which sort of gives you the complete picture.

Sameer Bhise: Sure those were my two questions. Thank you and all the best. Congrats…

Madhur Deora: It's the opportunity to also mention that we have shared in March 2022 when this issue first came up that we believe that the measures that were imposed by RBI on PPL will not impact Paytm's overall business and the fact that you see the MTU performance and then revenue growth performance of Paytm since then, it confirms that our initial assessment was correct and we don't see any material impact on Paytm's overall business during the course of the RBI measure of Paytm Payments Bank.

Sameer Bhise: Sure, that's helpful. All the best. Thank you.

Moderator: Next in queue would be Rahul Jain from Dolat Capital.

Rahul Jain: Yeah hi thanks for the opportunity and congratulations on very strong execution. I would just like you to help me on arriving at potential areas for us to get EBITDA neutral and beyond, so firstly from a payment processing charges perspective this is the first quarter where we see very little optimization in this line item as a percentage of payment services. So can we conclude that easy optimizations or relatively easy picking in this of cost item are behind us and it would be the run rate that we see right now, would be optimized further on a very smaller level. That is question number one. Second in this quarter we saw other marketing expenses seeing a big drop. So is that drop already baked in from a run rate point of view or some of the savings have come in the second half of the quarter so we would see this cost going down further in the upcoming quarter. And maybe in general, if you could share what would be the areas where we could see this savings coming incrementally ?

Madhur Deora: Yeah on your first question maybe I'll answer it at the contribution margin level Rahul. We do continue to obviously look for small and big opportunities to improve the profitability of each of our businesses. So we continue to do that, but I think it's fair to say that we went from a single digit contribution margin two years ago to 24% a year ago to 44% now. So clearly that trajectory was what we call the step change in contribution profit. We don't expect that or anywhere close to that pace to continue, but we do and will continue to look for opportunities to do certainly small improvements and not big improvements in each of our businesses. We do also expect to continue to benefit from some mix effects particularly from the lending business because lending is growing and is expected to continue to grow faster than our overall business. And lending has a higher margin than our payments business, for example so we do expect some mix effect, positive mix effect to come from that as well.

On your second question on marketing like we had mentioned in the last quarter, we did have a jump in marketing costs last quarter because of cricket sponsorships, because we had IPL as well as cricket matches last quarter. This quarter we did not have that and as a result our marketing costs went down. A chunk of marketing costs, not all, but a chunk of it is lumpy, right, especially when you start getting into sponsorships and so on. So we did not have that this quarter and we expect that at a lower level going forward. Having said that, I will say that if there are opportunities for us to invest in user growth, whether it is promotion, incentive, or marketing, which is having good ROI, we'll continue to do that. That will not take us away from our path to breakeven and our path to creating a long-term very profitable business. So we'll absolutely achieve that, but if there are opportunities for us to invest in efficient marketing whether it is through cashback or through ATL or through any other mechanism we would continue to do that and still achieve our profitability targets.

Rahul Jain: Right so just to conclude from your thought can we say that hereon optimization and profitability will be more revenue driven rather than cost optimization driven?

Madhur Deora: I think it's fair to say that revenue growth as well as growth of high margin revenue such as lending will be sort of the next big uplift to contribution profit. But I will point out that we have a large payments business, which is generating a significant net payment margin so even small improvements in that when they drop to the bottom line, they can be very significant from a bottom line standpoint, right? So if we are doing Rs. 443 crores a quarter of net payment margin, then even a 10-15% improvement can have a significant impact on the bottom line, right? So just, just because the number is actually now quite large and working on continuing to improve that number is a very high ROI for us.

Rahul Jain: Sure. Thank you and those were my questions.

Madhur Deora: Thank you.

Moderator: The next in the queue is Mr. Piran Engineer from CLSA.

Piran Engineer: Hi thanks for making my question and congrats on the quarter. Just on your lending business firstly on BNPL if I'm a customer who's paying some fee and I think one third of the customers were Delite customers don't pay any fee, how long does it take for me to get upgraded to a Delite customer status assuming that I don't default, of course?

Bhavesh Gupta: Hi Piran. Piran there is no time led formula. I think the different lenders have different appetites, but I could say between six to nine months of vintage of continuous performance and lenders revisit both the limit and the risk classification and there could be a set of customers who could be upgraded or downgraded. So it is not that once you're a Delite customer, you will remain a Delite customers. There is a small portion I would say, which is downgraded also, and you could also be upgraded. So it is a continuous process, but that ratio or the share of the Delite to Lite to many broadly remains range bound.

Piran Engineer: Yeah but that's also probably because you are still growing and a lot of your incremental customers will be say Lite and I just assume as customers mature over time maybe next two years or four years and of course if they're paying, you should have more Delite customers than Lite and if that happens and take rates reduce, will you pass it on to the banking partner or will we have to absorb it?

Bhavesh Gupta: So Piran it's a matter of conjecture, which is fairly long ahead of our time at this point in time. I do believe that two things will happen and I think I had mentioned this earlier. Number one, we don't see for at least a couple of years to come because just 4% of our MTU and MTU is also growing, that our new customer acquisition engine is going to slow down. And I just mentioned in a previous answer that we are seeing very robust growth every month now, more than 400,000- 450,000 users getting added to Postpaid. So we don't see that slowing down and hence the overall share of Delite, Lite etc will remain broadly range bound. The other thing that we also will see over a period of time is that the merchant looking at the impact of Paytm Postpaid to his sale, and hence increasing the MDR will also be a revenue opportunity, which will very easily offset any drop in convenience fee, if at all it was to happen. So that's the way the entire business model is going to play out. At this point in time the business model, at least for the next 12 to 18 months, I don't see any change in the business model albeit it may only have an increase in revenue, especially coming from MDR because more and more merchant acceptance, especially enterprise merchants resulting in higher MDRs is the trend that we're already seeing.

Piran Engineer: Okay that makes sense. And on your merchant loans, what would be the TAM of this business? I understand that about 1 or 2% of the merchants have a loan right now, but practically speaking what percentage of merchants are going to be onboarded on merchant loans, that's just one and one and a half lakhs…

Bhavesh Gupta: Sure. I think that's a very good question, Piran. The simple answer, the way we look at this piece is that merchant loans are derivatives of our devices merchant because largely 80% of our loans are given or taken by a devices merchant so we index our entire merchant business to devices merchant. Today their number is approximately at 4.8 million, growing about a million a quarter and what our belief is once a merchant has taken a device six months forward their probability of getting eligible becomes very high and give or take, we see about 50% of them keep getting eligible six months going forward. So as we continue to remain very bullish on adding more and more devices, we obviously remain very bullish in adding more merchant loans. Having said that, at current point in time, we have approximately 1.5 million merchants who are white listed to be given credit and have a pre-qualified offer on the app from various lenders, broadly amounting to about 2 billion US dollars of disbursement that we can do. So the current TAM itself is very large and as we are adding more devices, so the TAM will keep increasing.

Piran Engineer: Okay, so you said 2 billion dollars?

Bhavesh Gupta: Yeah, about 1.5 million, 15 lakh merchants are currently prequalified by lenders. Approximately as you know that the number is about one and a half lakh rupees per merchant. So that's the amount, about 15 to 20,000 crores of value.

Piran Engineer: Okay, got it. And just lastly in your earnings release you mentioned about some seasonality in the cloud business. If you can just sort of clarify what that was?

Madhur Deora: We mentioned seasonality in our commerce business and typically Q2 for entertainment is seasonally weak. In fact, we have said specifically for entertainment business as seasonality. So entertainment in Q2 is generally weak because of monsoons and so on. Also this particular quarter, not a regular season situation, but this particular quarter, the content line up was very weak and whichever sort of relatively good content that we had in movies also just didn't work as well as it was expected to. So as a result both movies and events had seasonally weak quarter.

Piran Engineer: No Madhur I get that. That was on commerce, but if you refer to your write up only, I don't know which page there's no page number here, but I think page 12 of the PDF, you say it's a seasonally strong quarter for PAI cloud and clearly it seems so because last three quarters your revenue was in the range of Rs. 190 to 220 crores and now shot up to 250.

Madhur Deora: Yeah I apologize. It shouldn't have said seasonally strong. It just was a strong quarter because cards did well, advertising did a little bit better, PAI cloud did well. So I think there, we didn't mean to say it was seasonally strong. It was just a strong quarter. Actually we have not said seasonally strong. We have just said it is driven by strong uptake in our credit card distribution. Yes, you're right and a seasonally strong quarter of a PAI cloud. It has nothing to do with the season. It's just to be a strong quarter.

Piran Engineer: Okay, okay. Fine,that clarifies it, thank you and all the best.

Moderator: Next question we'll take from Mr. Anand Bhavnani from WhiteOak. Anand Bhavnani you can unmute.

Anand Bhavnani: Thank you for the opportunity and congratulations for a good ramp up in the lending services business. If you could give us some colour on other financial services that you would want to explore as the lending business kind of continues to gain momentum and it's stabilized, what other financial services are on your priority list?

Vijay Shekhar Sharma: Anand we have Paytm Money, which is a stock brokerage and mutual fund distribution and we also have insurance distribution and brokerage business. So these two are other financial services businesses.

Anand Bhavnani: So on those can you give us some colour as to what you're targeting in terms of numbers and what kind of TAM?

Vijay Shekhar Sharma: We call them the future bets because there's a tremendous amount of technology development and brewing that it requires. So they are not materially large, as you can see, the numbers themselves are led by credit. Most of the revenue is driven by that.

Anand Bhavnani: Got it. Secondly on our expected credit loss in case of merchants, I see the number is higher than in case of Postpaid. So just wondering I would assume that merchants, because they're a lot more located on a particular spot and because they probably have a device and everything, they'd probably be less credit risk.

Vijay Shekhar Sharma: Anand when a loan is defined as a portfolio and lender side as a part of that definition of loan portfolio, they put expected credit loss as a number. It has nothing to do with actual credit loss. That credit loss is called net credit loss, meaning this is when you start a business, you say, this is my customer issue cost, this is my credit loss, this is my revenue so expected credit loss is a number that lender puts in definition of their book, of this kind of loss, which is actually nothing to do with whether the loan performance will be based on that or not. What you're seeking is net credit loss, which is in the presentation, and otherwise we always share as a detail in subsequent slides.

Bhavesh Gupta: And Anand if I can supplement over this piece, one they're two different products. BNPL is a 4500, 5000 rupees short term consumption credit for 30 days. The chance of default is far, far lower for everybody defaulting for 5,000 rupees whereas the merchant loan is a one year, 14 month, one and a half lakh rupee product through daily instalments deducted through pay settlements. So the IRR and the income that the lender makes are very different and what the customer pays in Postpaid is much lesser than what they pay in the merchant. So from a risk adjusted return merchant loan, even at a 5% expected credit loss while the actual credit loss as Vijay said is lower than that but expected credit loss, the return for the lender, return for Paytm is much higher versus a Paytm Postpaid.

Anand Bhavnani: Noted thank you much, all the best.

Madhur Deora: Thank you.

Moderator: Thank you Anand. The next question will be a repeat question from Mr. Vijit Jain. Vijit you can unmute your line.

Vijit Jain: Thanks Anuj. Just a housekeeping question alluding to one of the comments earlier made. So when a customer scans Paytm QR code to make UPI payment from a competitor app, in this instance, in this particular transaction, there is no scope for monetization, right? And is this particular transaction included in Paytm's UPI GMV when the regulator and NPCI reports it on their website?

Bhavesh Gupta: So Vijit, there is monetization definitely included. So if you're looking at monetization from a device subscription perspective or from a lending perspective, that monetization is agnostic to which app is being opened to pay to the merchant. It could be scanning from a competition app and paying a merchant. The merchant still needs a subscription service because he needs reconciliation at the shop and obviously that GMV that merchant is actually collecting is being processed through us and that is available to us to underwrite to our lending partners to give credit. So there is actually no problem and this GMV is called out as P2M GMV also in the definition of MPCI and hence is eligible for various kinds of incentives below 2000 rupees at different points in time.

Vidit Jain: Okay. Got it, thanks, thanks Bhavesh. That was my question.

Madhur Deora: Thank you Vijit.

Moderator: Thank you. And with that we come to an end of the Q&A session. As mentioned earlier, a recording of this call and the presentation and a transcript will be put online on the company website. So thank you all for joining.

Vijay Shekhar Sharma: Thank you namaskar.

Madhur Deora: Thank you everyone.

Bhavesh Gupta: Thank you everyone. Good day.