Investorstack Research Report

Northern Arc Capital Limited

What Northern Arc Capital Limited does

Northern Arc Capital is an RBI-registered NBFC built to serve the credit needs of Indian households and businesses that formal banks underwrite poorly or ignore. It sits between two worlds: on one side are millions of borrowers (MSME owners, rural women, urban consumers), and on the other are institutional investors (SBI, IFC, Goldman Sachs) seeking yield. Northern Arc originates, underwrites, places, manages, and services debt for this ecosystem. It does this through two distinct engines: a Direct-to-Customer lending business (MSME, consumer, rural) and a Credit Solutions platform (fund management, placement, and SaaS). Over its 17-year history, it has facilitated financing exceeding INR 2 trillion. As of March 2026, it manages Assets Under Management of INR 16,594 crore through a network of 360+ branches, 350 originator partners, and 1,300+ institutional investors.

> *"over the last 15 years, Northern Arc has very successfully navigated the multiple macroeconomic challenges including COVID, geopolitical disruption, MFI over- leveraging cycles, evolving regulatory landscape."*
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> MD, Q4 FY26 CONCALL (MAY 2026)

The core capability that took years to build is a data-driven risk engine. Proprietary scorecards (NuScore), an API-based lending platform (nPOS), and a 50-million-pixel data repository allow it to price risk accurately for segments where credit histories are thin. This capability is what makes its dual-channel model defensible. In D2C, it makes money lending directly. In Credit Solutions, it earns fees by offering this underwriting capability to partners. No other Indian NBFC is structurally identical.

Business segments

Direct-to-Customer (D2C) – MSME Finance (22% of AUM)

This segment provides secured Loan Against Property (LAP), supply chain finance, and mid-market loans to micro, small and medium enterprises. Average ticket size is approximately INR 11-15 lakhs. 100% of LAP loans carry a registered mortgage. The business operates through 69 branches across 7 states with over 550 employees. AUM in this segment grew 43% year-on-year to INR 3,691 crore as of March 2026. The growth is driven by branch expansion and productivity improvements. Portfolio quality is improving: X-bucket collection efficiency reached 99.4%.

Direct-to-Customer (D2C) – Consumer Finance (30% of AUM)

This is a digital lending business running through partnerships with fintech NBFCs under a First Loss Default Guarantee (FLDG) model. Northern Arc underwrites approximately 25,000-26,000 loans daily with an average ticket size of INR 50,000 to INR 5 lakh. The product is sticky: 70% of customers are repeat borrowers. AUM in this segment crossed INR 5,000 crore in Q4 FY26. The business benefits from regulatory clarity on FLDG issued by the RBI in February 2026, which removed a one-time provision overhang and stabilized the profitability trajectory. The business targets a risk-adjusted yield of 15-16%.

Direct-to-Customer (D2C) – Rural Finance (6% of AUM)

Northern Arc provides small-ticket Joint Liability Group (JLG) loans to rural women customers through its subsidiary Pragati Finserv. The average ticket is INR 30,000 to INR 75,000. The entire book is underwritten using the NuScore proprietary scorecard. 84% of the MFI book is covered under the CGFMU government guarantee scheme. The

business was consciously calibrated down from INR 1,500 crore to INR 900 crore during the MFI overleveraging stress of FY24-25. It has since been rebuilt, recording a record quarterly disbursement of INR 305 crore in Q4 FY26. The branch network expanded to 342 branches.

Credit Solutions (41% of AUM – includes Intermediate Retail, Fund AUM, and Off-book)

This is the capital-light ecosystem enabler. It encompasses performing credit funds (AIFs and PMS) with AUM of INR 3,092 crore, placing INR 11,834 crore of structured debt in FY26, balance sheet lending to originator partners (Intermediate Retail), and SaaS offerings (nPOS, NuScore, Nimbus, Altifi). The funds have a weighted average XIRR of 14.57% with zero capital loss to investors across 6 closed funds. The Altifi bond platform has over 80,000 registered investors. This segment provides sticky fee income that complements the balance sheet lending yields.

Products and business detail

Secured Loan Against Property (LAP): The flagship MSME product. Average ticket INR 11-15 lakhs, LTV capped at 50-60%, FOIR at 50%. "100% registered mortgage structure" ensures a perfect collateral. This means Northern Arc can underwrite based on estimated income while holding a hard asset guarantee.

Supply Chain Finance (SCF): Finances suppliers and buyers across value chains in agriculture, logistics, metals, manufacturing, textiles, and retail. AUM stood at INR 228 crore as of March 2025 across 30 customers.

Consumer / Digital Personal Loans: Short-tenure loans for consumption needs. Distributed through partner fintechs under FLDG (5% credit loss cover). "We've consciously avoided short tenure portfolio to almost zero one." The shift is toward stickier loans of 15-18 months.

Krushi JLG Loans: Joint Liability Group loans to rural women. Ticket size INR 30,000-75,000, coupon rate of 24.9%. "100% of our rural loans are written, underwritten using our proprietary score card called Nu Score."

Performing Credit Funds (AIF & PMS): Funds investing in debt instruments of financial institutions. Investors are HNIs, UHNIs, family offices, corporates, DFIs, and offshore investors. The fund management business is scaling with new thematic funds in climate, MSME, and women entrepreneurship. Six funds have closed, all delivering ahead of target.

Altifi Bond Platform: Registered OBPP platform with BSE and NSE. Allows retail/HNI investors access to bonds, securitised assets, and AIF units. Over 80,000 registered investors as of May 2026. Serves as a direct distribution channel for Northern Arc's sponsored debt products.

nPOS Platform: API-based on-lending and co-lending platform enabling straight-through processing. "Processed over 2.5 lakh loan assessment requests in FY25, facilitating disbursals exceeding INR 10,000 crore." Being extended to external banks (South Indian Bank partnership).

NuScore: Proprietary machine learning-based underwriting scorecard. Built on 50+ million data points. Offered as analytics-as-a-service. Used by 2-3 external financial institutions with more in the pipeline.

Buying Relationship: *Who decides?* For LAP, the branch credit officer and central underwriting team. For consumer finance, the fintech partner selects the customer; Northern Arc sets the risk filters. For fund investors, the decision is made by CIOs and investment committees based on track record and XIRR. *Why pick Northern Arc?* For partners: access to stable, low-cost capital and a sophisticated tech stack. For borrowers: speed of disbursal and accessibility. For investors: a 15-year track record of zero capital loss across credit cycles. *Switching Costs:* High for partner institutions (tech integration, trust). Low for individual D2C borrowers. *Concentration:* Granular. Underwriting limits restrict any single district or partner exposure to 5-26%, preventing event-driven blowups.

Customers

Northern Arc serves a layered customer base.

19.89 lakh Direct Borrowers: These are the end users. MSME owners taking secured LAP (approx. 9,800 of them), rural women in JLG groups (3.91 lakh active), and urban consumers accessing digital loans (14 lakh). 70% of consumer finance customers are repeat buyers. 26% are first-time borrowers entering the formal credit system.

350 Originator Partners: These are NBFCs and financial institutions that originate retail loans. "90% of our partners are rated BBB and above." "95% having capital adequacy of more than 20%." They are the core of the Credit Solutions ecosystem. They rely on Northern Arc for funding (balance sheet and placement) and technology (nPOS). This relationship is hard to replicate.

1,300+ Institutional Investors: This base includes Goldman Sachs, DCB Bank, SBI, Citi Bank, FMO, IFC, and ADB. Northern Arc places securitization pools and fund units into this base. "We placed almost INR10,000 crores of securitization deals in the market last year."

80,000+ Altifi Registered Investors: Retail and HNI investors accessing the bond platform.

Competitive landscape

Northern Arc operates in multiple, overlapping competitive arenas. In MSME LAP, it competes with banks (SBI, HDFC) and large NBFCs (Bajaj Finance, Piramal). The market is highly crowded on pricing and speed. Northern Arc avoids the micro-ticket segment (sub-INR 7 lakhs) and the 24% yield chase. It targets a niche: "estimated income with a perfect collateral." This keeps competition somewhat bounded.

In consumer digital lending, competition is intense from both fintechs and incumbents. Northern Arc's edge is risk underwriting discipline and the ability to price for risk using its data models. The FLDG structure provides a buffer. Many competitors lack this data depth or the discipline to walk away from high-yield cohorts. "We ensure irrespective of what kind of the loan is, it goes through our proprietary scorecards."

In rural finance, Northern Arc competes with large MFIs (Bandhan, CreditAccess). It is a smaller, more agile player with a tech-first approach (NuScore) and 84% CGFMU cover.

The unique competitive position is the Credit Solutions segment. "The unique strategic posture which Northern Arc has is hitherto no other company have." (MD, Oct 2025 concall). No other NBFC has a comparable combination of an on-book D2C lending business, an off-book fund management business with a decade of zero-loss track record, a direct institutional placement franchise, and a retail bond platform. This "butterfly effect" of capabilities creates a moat that is hard to replicate. The biggest risk is not a single competitor but a synchronized credit downturn that tests all channels simultaneously.

Industry

India's retail credit market is valued at INR 82 trillion (FY 2024-25), growing at a 15% CAGR over the last seven years. The NBFC sector has outpaced broader credit growth, expanding at a 13.2% CAGR and projected to reach INR 77 trillion by FY 2027-28.

The demand drivers are structural. Household consumption nearly doubled to USD 2.4 trillion between 2014 and 2024 and is expected to reach USD 3.4 trillion by 2030. This creates massive demand for consumer finance. The MSME sector faces a credit gap of INR 117 trillion against a total demand of INR 159 trillion. Only INR 42 trillion is currently served formally. Rural India remains deeply underpenetrated. These are Northern Arc's core markets.

Regulation is a powerful shaper of the industry. The RBI's repo rate cuts from 6.5% to 5.5% have eased the cost of funds. The February 2026 FLDG circular provided clarity on credit enhancement accounting, directly benefiting Northern Arc's consumer finance model. The restoration of standard risk weights on bank exposures to NBFCs (effective April 2025) improved the availability of bank financing. In microfinance, the MFIN and Sa-Dhan guardrails aim to prevent the overleveraging that caused the FY24-25 stress cycle. CGFMU coverage provides a safety net.

Cyclicality is embedded. The MFI sector saw its portfolio shrink by ~30% due to overleveraging. The Karnataka microfinance ordinance caused a spike in delinquencies. Unsecured business loans and small-ticket LAP segments are showing stress. "Stress continues to build in the unsecured business loan and small-ticket lap segments." (MD, Q3 FY26 concall). Monsoon outcomes, geopolitical tensions (West Asia), and interest rate cycles directly impact portfolio quality and credit demand.

India is not an "import substitution" story for credit; it is a "formalization of credit" story. NBFCs like Northern Arc are replacing moneylenders, not imports. The country's low household credit-to-GDP ratio (~25%) relative to peers points to a sustained growth runway, but one that will be punctuated by credit cycles. This structural trend is the bedrock of demand for Northern Arc's products. The company's guidance is to grow at 3x GDP (22-25% AUM growth), reflecting management's confidence in this tailwind, albeit with an explicit acknowledgement of the cyclical headwinds.

Growth triggers

- **Regulatory clarity on FLDG for digital lending** – RBI guidelines issued in February 2026 now permit NBFCs to factor in cash collateral as FLDG for ECL computation. This removes the one-time provision overhang that impacted profitability in FY25 and provides stability for the consumer finance business going forward. (Q4 FY26 concall, May 2026)
- **RBI repo rate cuts and supportive monetary policy** – A cumulative 100 bps rate cut from December 2024 to June 2025 is improving borrowing costs. With 60% of borrowings linked to variable rates, Northern Arc is well-positioned to benefit from further transmission as MCLR resets continue. This supports both NIM expansion and credit demand. (Q1 FY26 concall, Jul 2025; Q2 FY26 concall, Oct 2025)
- **MSME credit gap opportunity** – The MSME sector still faces an addressable credit gap of nearly 24%, estimated at about INR 30 lakh crore. Northern Arc's MSME portfolio grew 43% YoY to INR 3,691 crore as of March 2026, driven by 17 new branches added in FY26 and improved productivity. The company sees this as a long-term annuity franchise. (Q4 FY26 concall, May 2026)
- **MFI sector revival** – The microfinance book is showing clear recovery signs. Incremental PAR 0+ accretion has reverted to pre-stress levels. Collection efficiency improved from 98.7% in September 2025 to 99.6% in March 2026. Record quarterly rural disbursement of INR 305 crore in Q4 FY26. 84% of the MFI book is now covered under CGFMU guarantee, providing strong downside protection. (Q2 FY26 concall, Oct 2025; Q3 FY26 concall, Jan 2026; Q4 FY26 concall, May 2026)
- **Household consumption growth** – Indian household consumption nearly doubled to USD 2.4 trillion during 2014 to 2024, and is expected to reach about USD 3.4 trillion by 2030. This creates a structural tailwind for consumer finance, which grew 39%+ YoY and now represents 30% of AUM. (Q4 FY26 concall, May 2026)
- **D2C mix improvement toward 65%+ target** – The direct-to-customer share of AUM increased from 19% in FY21 to 59% in FY26, driving NIM expansion of 380 bps from 5.6% to 9.4%. Management targets a 65% D2C mix, which is expected to expand NIMs by another 30-50 bps and improve ROA. (Q4 FY26 concall, May 2026)

- **Fee franchise scaling** – Placement volumes of INR 11,834 crore in FY26, fund management AUM of INR 3,092 crore, and the Altifi bond platform with 80,000+ registered investors are building a capital-light fee income stream. Placement fee income grew 22% YoY to INR 31 crore. New funds and platform expansions are in the pipeline for FY27. (Q3 FY26 concall, Jan 2026; Q4 FY26 concall, May 2026)
- **GST rate cuts and festival season demand** – Government stimulus through GST rate reduction provided a flip to consumption in H2 FY26, creating a supportive environment for credit growth. This momentum extended into October 2025 and beyond. (Q2 FY26 concall, Oct 2025)

Key risks

- **Geopolitical tensions in West Asia** – A direct exposure of less than 2% of the MSME book to sectors like gas, petrol, chemicals, and pesticides limits immediate impact. But indirect macroeconomic effects—commodity price spikes, supply chain disruptions, and business sentiment—could affect MSME borrowers' repayment capacity across a broader portfolio.
- **Weather and monsoon uncertainty** – The rural finance portfolio is seasonally dependent on agricultural cash flows. Adverse monsoon patterns or extreme weather events could compress rural incomes and raise delinquency rates in the Krushi JLG book, which is still recovering from the recent MFI stress cycle.
- **Credit quality deterioration in unsecured business loan and small-ticket LAP segments** – Industry-wide stress in these segments continues to build. Northern Arc has some exposure through its intermediate retail book and its own balance sheet. If stress deepens, credit costs could exceed the guided range of 2.7% to 2.8%.
- **Regulatory changes in microfinance and digital lending** – The MFI sector is seeing new guardrails from MFIN and Sa-Dhan. Changes to CGFMU coverage terms, digital lending FLDG guidelines, or new restrictions on partnership models could alter the growth trajectory and provisioning requirements for the rural and consumer finance books.
- **Rising interest rate environment and liquidity tightening** – With 60% of borrowings on variable rates, a reversal of the current rate-cutting cycle would compress NIMs. Tightening liquidity could also increase borrowing costs and reduce the company's ability to raise debt at competitive rates, particularly if bank lending to NBFCs slows.
- **Borrower overleveraging in microfinance and consumer segments** – The MFI industry portfolio already shrunk by ~30% from INR 4,16,000 crore to INR 3,23,000 crore due to overleveraging stress. If multiple lending to the same borrowers continues unchecked in either rural or consumer segments, default risk could re-escalate.
- **Concentration risk in partner-based models** – The consumer finance business depends on digital lending partners for customer acquisition and collections. The intermediate retail book depends on 350 originator partners. If any significant partner faces financial or regulatory difficulties, it could disrupt collections, asset quality, and business continuity.

Walk the talk

Northern Arc has built a track record of setting measurable targets and delivering against them, even in a volatile operating environment. The most instructive example is the credit cost guidance journey through FY26.

In the Q1 FY26 concall (July 2025), management said:

> *"we expect H2 credit cost to land somewhere between 2.7% to 2.9%"*

At the time, Q1 credit cost was 3.0% and the MFI stress was still elevated. By Q2 FY26 (October 2025), credit cost had already improved to 2.7%, and management tightened the guidance further:

> *"expect credit cost to remain stable in the range of 2.6% to 2.8% in the second half of the year"*

Q3 FY26 (January 2026) saw a spike to ~3.0%, partly due to a one-time INR 23 crore provision on the digital lending book. But management stayed transparent about the cause and reiterated confidence. The full-year outcome in Q4 FY26 (May 2026) vindicated the guidance—full-year credit cost ended at 2.8%, right in the middle of the original range.

Similarly, the AUM growth guidance of 20%-22% for FY26, set in Q2 FY26, was achieved exactly—AUM grew 22% YoY to INR 16,594 crore as of March 2026.

The ROA guidance tells a similar story. In Q2 FY26, management targeted "a ROA of 2.8%" for FY26. Full-year ROA came in at 2.8%, with Q4 FY26 hitting 3.3%. Management then set a new benchmark:

> *"our objective is to get to 3 plus return on assets and like we said over the next 8 to 10 quarters, get to mid-teens and late-teens ROE"*

Q4 FY26 ROA of 3.3% already crossed the 3% threshold, and ROE reached 14%. The path to mid-to-late teens ROE is now visible through the D2C mix shift, fee franchise scaling, and improving credit costs.

The consistency between guidance and outcomes across credit cost, AUM growth, and ROA in a year with multiple headwinds—Karnataka MFI ordinance, FLDG regulatory uncertainty, West Asia tensions—suggests that management's forecasting discipline is genuine, not aspirational.

Scenarios

Bull case

The economy stays on a steady growth path, household consumption continues its trajectory toward USD 3.4 trillion by 2030, and the MFI sector fully normalizes. Northern Arc's D2C mix crosses 65% within 18 months, driving NIM expansion beyond 10%. Credit costs stabilize at 2.5% or lower as the high-quality new vintages in MSME and consumer finance mature without incident. The fee franchise—Altifi bond platform, fund management AUM, and placement volumes—scales rapidly, adding 100-120 bps to the loaded NIM. The rural finance book, now 84% CGFMU-covered and originated through NuScore, scales back to INR 1,500 crore+ without a repeat of the stress cycle. ROA sustains above 3.2%, and the balance sheet grows at 25% annually, driving ROE toward 17-18% within 8-10 quarters.

Base case

The operating environment remains mixed. Consumption grows, but geopolitical tensions and monsoon uncertainty create periodic stress pockets. Credit costs stay within the guided 2.7% to 2.8% range. AUM grows at 22-25% annually, in line with the stated 3x GDP growth target. The D2C mix gradually improves to 62-63% over the next two years, contributing modest NIM expansion. The fee franchise grows steadily but not explosively—placement volumes track securitization market activity, and fund management AUM increases as new thematic funds are launched. Rural finance scales cautiously, with management maintaining tight underwriting discipline and CGFMU coverage. ROA holds at 2.8-3.0%, and ROE trends toward 14-15% over the next 6-8 quarters. This is a steady compounding story, not a step-change.

Bear case

The macro environment deteriorates. West Asia tensions escalate, driving a sustained commodity price shock that stresses MSME cash flows. Monsoon failure hits rural incomes hard, sending the MFI book back into stress despite CGFMU coverage. The unsecured business loan and small-ticket LAP segments, already under pressure across the industry, see further deterioration that impacts Northern Arc's intermediate retail book. Credit costs spike to 3.5% or higher, compressing ROA below 2.5%. AUM growth slows as management pulls back on disbursements to protect asset quality. The consumer finance book, while FLDG-protected, sees elevated delinquencies that strain partner relationships. Cost of funds rises as liquidity tightens and the RBI reverses rate cuts. The D2C mix improvement stalls as growth in the highest-yielding segments is curtailed. ROE stagnates in high single digits, and the stock trades at a discount to book as the market prices in a prolonged earnings trough.