Reliance Capital Limited

Q1 FY17 Earnings Conference Call

16th August, 2016

SPEAKERS: Management of Reliance Capital

Moderator: Good morning ladies and gentlemen, welcome to the Reliance Capital Limited Q1 FY17 post earnings conference call hosted by Reliance Securities Limited. As a remainder all participant lines will be in the listen only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal the operator by pressing '*' and '0' on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Asutosh Mishra from Reliance Security, thank you and over to you sir.

Asutosh Mishra: Good morning everyone and welcome to the Reliance Capital Post Earnings Conference Call. Today, we have with us Mr. Sam Ghosh - ED and Group CEO of Reliance Capital, along with the entire senior management team to discuss Q1 FY17 Earnings and Strategy on the key operative business going forward, over to you sir.

Sam Ghosh: Thank you Asutosh, good morning to all of you and welcome to Q1 FY17 Earnings Conference Call. We have the CEOs from all our businesses with us, Mr. KV Srinivasan from Reliance Commercial and Home Finance; Sundeep Sikka from Asset Management Business, Rakesh Jain from Reliance General Insurance, Gopkumar from the Broking & Distribution Business; we also have with us, Sunil Agarwal, CFO of the Life Insurance business, as well as Reliance Capital CFO - Mr. Amit Bapna.

Let me present a brief summary of per consolidated results and an update on each of our business, after that we will take questions.

In this quarter the total income increased by 49% to Rs. 37 billion, the consolidated net profit for the quarter rose by 3% to Rs. 2.1 billion. In the last financial year, Reliance Capital received a dividend from Reliance Life. As this year, Reliance Life is consolidated, excluding this one off profit, Reliance Capital profits are up 33% from last year. Core business profits were driven by higher earnings in the Asset Management, General Insurance and Commercial Finance segments; however, Life Insurance business had a breakeven quarter as against the profit of Rs. 352 million in Q1 FY16. The net worth of Reliance Capital increased by 13% Rs. 156 billion as on June 2016.

In Reliance Commercial Finance assets under management increased by 17% to Rs. 165 billion. Net interest margin rose from 6% to 6.8% in Q1 FY17. In Reliance Home Finance, assets under management increased by 32% to Rs. 83 billion. Profit before tax for the quarter was Rs. 301 million. In asset management, our Mutual Fund average assets under management grew by 15% to Rs. 1.7 trillion, with a market share of 11.6%. We remain the 3rd largest player in the mutual fund industry. Profit before tax grew by 13% to Rs. 1.2 billion driven by higher mutual fund AUMs. In the life insurance business, renewal premium rose by 4% to Rs. 5 billion in this quarter. Persistency improved from 56% to 60% for the quarter ended June 2016. In general insurance, we are amongst the top 5 players in the private sector. Gross written premium increased by 5% to Rs. 9 billion. Profit from the business rose by 23% to Rs.

363 million. We have given detailed financials and operating parameters for each of our major businesses in our presentation and review report. I will now go through the main highlights in each business:

Reliance Commercial Finance, a division of Reliance Capital, continues to focus on secured asset lending to niche segments of SME, Infrastructure financing, Loan against property, and Commercial Vehicle loans. Disbursements increased by 10% to Rs. 17 billion. The assets under management grew by 17% to Rs. 165 billion. The outstanding loan book rose by 20% to Rs. 123 billion. We securitised loans worth Rs. 8 billion during the quarter - an increase of 15%. At the end of the quarter, 100% of the book continued to be secured. The total income for the quarter increased by 14% to Rs. 5 billion. Profit before tax rose by 36% Rs. 572 million driven by higher asset growth, increase in margins and lower operating costs. The return on equity for the quarter rose to 9.2%. The net interest margin rose from 6.0% to 6.8% in Q1 FY17, supported by lower funding costs. The cost to income ratio improved from 17.1% to 16.3% for the quarter. The gross NPAs were Rs. 5.6 billion as on June 2016, i.e. 3.4% of the assets under management, on a 90 day basis. As the Commercial Vehicle industry remains under stress, the business intends to continue to reduce its exposure in this segment. The coverage ratio, including write-offs, at end of June 2016 stood at 58%. Excluding write-offs, the ratio was at 23%.

Reliance Home Finance Limited is a 100% subsidiary of Reliance Capital and caters to the self employed segment in the mortgage sector. We will continue to grow our housing finance assets in a significant manner in the future. The assets under management grew by 32% to Rs. 83 billion. In Q1 FY17, disbursements increased by 54% to Rs. 16 billion. The outstanding loan book rose by 40% to Rs. 78 billion. The total income for the quarter increased by 28% to Rs. 2 billion. The profit before tax decreased by 20% to Rs. 301 million due to higher operating expenses, as the company continues to invest towards expanding its scale and operations. The cost to income ratio rose from 13.2% to 16.0% for the quarter. The net interest margin for the quarter was largely stable at 4%, even as we expand our portfolio towards the lower ticket-affordable housing business. The return on equity was 15.3% for the quarter, as compared to 20% in Q1 FY16. As on June 2016, the gross NPAs remained flat at 1%. The coverage ratio, including write-offs, at end of June 2016 stood at 33%. Excluding write-offs, the ratio was at 24%.

Reliance Nippon Life Asset Management manages Rs. 3.0 trillion of assets across its mutual fund, pension funds, managed accounts, offshore funds and alternative investment funds. Reliance Nippon Life Asset Management is the largest Asset Manager in India. Reliance Mutual Fund is amongst the top three mutual funds in India, with a market share of 11.6%. The average assets under management of Reliance Mutual Fund were Rs. 1.7 trillion as on June 2016 - an increase of 15%. The number of systematic investment plan and systematic transfer plan folios rose by 5% to 1.4 million, indicating continued participation in equities by the retail investors, despite challenging market conditions. For the quarter ended June 2016, Reliance

Mutual Fund registered the highest absolute growth in retail AUMs amongst the top 5 asset management companies, as compared to March 2016. As on June 2016, Reliance Mutual Fund has the highest AUM sourced 'outside the Top 15 cities' in the industry. On the qualitative front, the Company managed to create key differentiators as compared to its peers. Reliance Mutual Fund launched an industry-first initiative called 'Instant Redemption' through which investors can redeem and have funds credited to their bank account within 30 minutes. Also, Reliance Mutual Fund has the lowest 'complaint-to-folio' ratio amongst the top 5 asset management companies. Despite volatile capital markets, income for the quarter ended June 30, 2016, remained stable at Rs. 3 billion. The business achieved a profit before tax of Rs. 1.2 billion - an increase of 13%. Reliance Mutual Fund continues to be amongst the most profitable mutual funds in India. Return on equity was 22% for the quarter ended June 2016.

In Reliance Nippon Life Insurance, new business premium was Rs. 2 billion, while renewal premium increased by 4% to Rs. 5 billion. Individual WRP decreased by 31% to Rs. 1 billion. The industry growth continued to be driven by ULIP products. Being an agency-driven insurer, we continue to stay focused on the traditional product segment, which formed 82% of the Individual New Business Premium in Q1 FY17. Also, premium declined due to our strategy of creating a larger distribution base, instead of a few high performers. Overall persistency rose from 56% to 60% in Q1 FY17. The business continues to focus on Agency and proprietary channels, which have better persistency. Continued growth in renewal premium, along with higher persistency, demonstrates our emphasis on improving the business quality. The business posted a marginal profit in the quarter, after the exceptional loss in Q4 FY16 due to strengthening of reserves. Total funds under management were at Rs. 158 billion as on June 2016. Sum assured of policies in force was Rs. 989 billion. There are 3 million policies in force. There is a network of over 800 offices and approximately 77,000 active advisors across India. Reliance Nippon Life Insurance has successfully commenced relationship with over 8 financial institutions in the bancassurance space. Also, we are in active discussion with more players in the sphere of Schedule Commercial Banks, to expand this channel further. With support from the bancassurance channel, improved persistency and higher agency productivity, we expect to continue the profitable trend and regain the market share in the private sector.

Reliance General Insurance is amongst the top 5 private sector General insurance companies in India - in terms of gross premium - with a private sector market share of 7.5%. The Gross Written Premium for the quarter was Rs. 9 billion - an increase of 5%. The business continues to defocus on the third party motor business, on a standalone basis, as well as commercial vehicles. Premium from preferred segments such as private cars, two wheelers, health and travel continued to grow in line or better than the industry. The combined ratio declined marginally from 115% to 114% in the quarter. The combined ratio for the short-tail business touched 100%. Going forward, with the planned reduction in the motor third party business, we expect the ratio to improve further. Our focus in this business has been to improve profitability, while maintaining our market position. Profit for the quarter increased by 23% to Rs. 363 million. For the quarter ended June 30, 2016, the return on equity rose to 13%. As on

June 2016, we have the largest agency force in the private sector with over 21,500 retail agents and more than 125 branches. In Q1, Reliance General Insurance concluded distribution tie-ups with key financial institutions, including IndusInd Bank, Bank of India, Indiabulls Housing Finance and SVC Bank. Also, the company aligned itself with nine automotive manufacturers. The Company is under discussion with several other institutions for similar tie-ups. These partnerships will provide a significant impetus to the business growth in the coming quarters.

Reliance Securities is amongst the leading retail equity broking houses in India. Also, it is amongst the leading distributors of financial products and services in India, with a network of over 160 branches. The focus in this segment is on the key business verticals of broking, distribution and wealth management. The equity broking accounts increased by 3% to over 780,750. And the average daily equities turnover rose by 31% to Rs. 24 billion. The number of commodities broking accounts rose by 10% to over 65,750. The daily average commodities turnover was Rs. 4 billion - an increase of 33%. In wealth management, the assets under management stood at Rs. 28 billion - an increase of 66%. For the quarter, total income declined by 3% at Rs. 542 million. The business had a profit of Rs. 3 million as against a loss of Rs. 169 million in Q1 FY16. Going forward, we expect to continue the trend of profitability.

Reliance Asset Reconstruction is in the business of acquisition, management and resolution of distressed debt and assets. As on June 2016, the assets under management rose to Rs. 15 billion - an increase of 29%. The profit before tax declined to Rs. 16 million due to lower acquisitions during the quarter. Consequently, return on equity decreased to 3% as against 9% in Q1 FY16. We expect to accelerate the acquisitions in the coming quarters with improving market conditions and asset sales by the banks.

In conclusion, I would like to say that all our co-businesses are on track in terms of operating performance and we expect each of our business will continue the trend of profitable growth on a consistent basis. Thank you very much, we can now take questions.

Moderator: Ladies and gentleman, we will now begin the question and answer sessions. We will take the first question from the line of Manish Shukla from Deutsche Bank. Please go ahead.

Manish Shukla: First on consol financials, could you please give the breakup of 293 crores of capital gains and dividends for this quarter. In terms of what is the dividend income portion and what is the capital gains portion.

Management: Those will be dividends which have been primarily received by Reliance Life because Reliance Life is a consolidated entity now and dividends received from their assists under management would also be reflected in the consol numbers.

Management: I think it is difficult to look at this year Q1 to Q1 because last year we did not consol Life and this year we are consolidating Life.

Manish Shukla: Okay, so just to understand it clearly that is Q1 FY16, Reliance Capital would have received some dividend from Reliance Life right.

Management: Correct, right.

Manish Shukla: And this year Reliance Life dividend itself are getting consolidated.

Management: Yes, so it won't be there in the consol numbers then. So it is a line by line consolidation this time. You know the asset management dividends were always not part of consol because they used to get knocked off. In case of Life Insurance, they were part of consol numbers till last year. This year they get knocked off again because it became a subsidiary.

Manish Shukla: Sure, then on the home finance business, over the last one year the margins are down almost 50 basis points, that in an environment where the funding cost has been only coming down seems very counterintuitive two so what explains the margin contraction for the home finance.

Management: See couple of things, one is the percentage of our AUM which is currently coming in from the affordable housing has gone up now and plus the disbursement themselves have grown significantly and if you look at YOY disbursements have gone up by about 54%. In the home finance business, typically, the upfront cost of underwriting and taking onboarding a case tend to be significantly high so that is what is getting reflected in the lower profits but broadly the point is that this should be seen more like an investment for the future rather than as a margin reduction.

Manish Shukla: Now I appreciate that on the OPEX front, it is just that the against the 54% kind of a disbursement growth, NII growth is only 4%. So that does not make any sense, that kind of a disconnect between disbursement growth and NII growth and the funding costs are coming down. I understand the OPEX part.

Management: This is what I am saying the ratio of affordable housing that is coming in as part of the total book or the total disbursement that has also gone up.

Manish Shukla: What would be your release on that segment?

Management: That typically we do that on an average of around 10% or so, so you will get a net interest margin of somewhere in the region of around 2 to 2.5%.

Manish Shukla: Okay, alright. The next question is on Life Insurance. On Life Insurance, the AUM contraction seems to be fairly large, let me make myself a little clear, if I were to add your total premium for the last four quarters that is September quarter to now it comes to 43 billion, whereas the AUM is actually down by a billion or so. So I am saying there seems to be some serious run off on the Life Insurance AUM or is my understanding incorrect here?

Management: There are two things – one is our continued focus on traditional policy so typically in traditional business, the contribution to AUM in the initial years is very-very low. Therefore, the growth of the AUM would be very-very slow in the first 2-3 years of the policy. Secondly, because of the past ULIP business that we did and the lock-in period getting over a 5 years and markets are performing and therefore there is a huge surrender that is happening. We are also focusing on surrender retention by dedicating a full team so whoever comes for surrender we are trying to retain those customers but having said that this is largely due to the focus on traditional business.

Manish Shukla: But at the same time the equity market and bond markets both have rallied right, so that should have been a tail way end because of mark-to-market on AUM from that itself.

Management: To that extent, market-to-market for ULIP business is there but as I said in the traditional business, the contribution to the AUM is very slow and the valuation of non-equity for traditional is different than a ULIP, so that really does not matter the non-equity portion in the traditional business does not matter as far as the market-to-market are concerned.

Manish Shukla: No I am saying only about the debt equity within the ULIP book.

Management: Within ULIP, there is a surrender that is happening, due to which the AUM is declining.

Moderator: Thank you. We will take the next question from the line of Nishchint Chawathe from Kotak Securities. Please go ahead.

Nishchint Chawathe: Just one question from my side and that would be on your outlook for premium growth in the life business. I know that there is a change in the business mix but you know at what time does it really start stabilizing and what would be the outlook over here for next 4-6 quarters?

Management: As you rightly observed there is a decline in the individual WRP, this is due to our defocusing from the TPD channel so we are doing away with the partners who are not contributing quality business to us. So we have stopped doing business with them. Secondly, we have changed our agency plan starting this year so we are focus more on activities and building a quality book, and we are focusing on creating a larger distribution base rather than focusing on a few good performers, so the earlier focus was on bringing up better performance from a few set of agents but now we are engaging a larger agency base on a daily basis in our various branch offices which will give us a good result in a longer term. So I see the numbers going up from H2 onwards which is the second half of the year, and we have planned it accordingly itself for this financial year.

Moderator: The next question is from the line of Ashwin Balasubramaniam from HSBC Asset Management. Please go ahead.

Ashwin Balasubramaniam Yes I have a couple of question in the commercial finance business, first is if I look at the disbursements this quarter this seems to have gone down, but if I look at the AUM it is still actually gone up on a quarter-on-quarter basis quite substantially and I mean the repayment seem like quite very low in fact I mean if I compare it to past trend so just trying to understand that disconnect there, because is there any buyout or something which is also there which is included as a part of AUM? Secondly, the segment-wise yields which you have given between June and March that seems to be the fair bit of movement across all the segment so I think in LAP and SMEs you have seen some decrease and the other way around in CV so if you can give some sense of how the yields have moved in the various segment that will be helpful, thanks?

Management: Disbursements have increased by about 10% or so but the AUM has gone up a little higher than that, simply because of the pre-closures having come down fairly because this is one thing that we have been focusing upon in terms of retention of the customers, etc., because you know post the removal of the pre-closure charges, there was a spike in the premature closure of loan so that trend seems to have gone down. Plus, what has happened is that the retention efforts that we have put in has actually resulted in much better customer retention so therefore the AUM growth is little higher than what your disbursement figures will suggest.

Ashwin Balasubramaniam I am looking at on a Q-O-Q basis so last quarter the AUM was 151 billion and in Q1 you have disbursed 16 billion so if I add that up that comes to about 168 so only 4 billion has run down as compared to in the past it has been like much higher.

Management: Yes, which is true. Substantial part of run down effectively used to come from pre-closure etc. See other thing is that as far disbursement is concerned you cannot compare Q4 and Q1 there is a significant seasonality factor which is involved. So, on a full year basis, I do not think we do more than 15% of the business in Q1, while almost 40% happens in the Q4. So on the margin side there is not very significant movement across the board. I think they are more or less in a stable environment except that we might have made some small changes as far as the customer focus is concerned in some of the sub-segment, so that could be this thing.

Ashwin Balasubramaniam Okay and on the Home Finance, which is also the yields have moved quite a bit right I mean if I look at the home loan part I think it has come down from about 11.5% to 10.6% so again is there change on the customer profile or it is just a margin sort of compression which is there in the segment?

Management: Yes, okay, see overall what has happened is the older book which was the higher yielding book is running off so therefore which is getting replaced at a faster pace by the new book because we are now disbursing far greater amounts today than what we used to do about 2 years or 3 years earlier. So the impact of the new book which is obviously coming in at a much lower interest rate is reflected in the overall margins. Second factor as far as the overall business itself is concerned the business mix has changed in favor of home loans versus construction finance or a LAP so that will automatically depress the interest margins in the interim which obviously will get nullified over a period of time because of the stability factor which is associated with home loans. Number 2, the risk weightages of home loans being little lower than what you will find for LAP or construction finance, so that will have a positive impact on the ROE going forward.

Ashwin Balasubramaniam: Okay and just one last question this is in terms of I think once the Reliance Commercial Finance becomes as a separate entity, the loans would move from the Reliance Capital to Reliance Commercial Finance and Reliance Capital will be more of a holding company is that right?

Management: Correct, it will be a CIC. Reliance Capital will apply to become a CIP yes.

Ashwin Balasubramaniam: Sir I had one question with regard to this so will the currently we also have some non-core investments and also some corporate loans will have capital those will also move to Reliance Commercial Finance?

Management: What we will do is some of the corporate loans, etc., we will obviously try and bring them bring them down significantly. As per CIC guidelines, 90% of our exposure has to be in group companies, and 10% could be third party investments. So, that is what that we will comply with. Our aim is that, as soon as we complete the Commercial Finance demerger by October, between October and January, we will complete all the changes in Reliance Capital, so that we are in compliance with CIC guidelines.

Moderator: We will take the next question from the line of Anita Rangan from HSBC Asset Management. Please go ahead.

Anita Rangan: Well, sir just wanted to get a sense on how the NPLs are in both the commercial finance and the house finance segment on the net basis and also if you can get a sense on what the NPA recognition norms are in the commercial finance segment?

Management: Yes, NPAs on a YOY basis have marginally improved from 3.7 to 3.4. Our recognition norms have always been at 90 days so we do not have any impact on us as far as the change in the RBI guidelines are concerned, so we have always recognized them at 90 days. But, broadly speaking, I would expect the NPL to be more or less stable, maybe 15-20 basis points up and down would be the kind of quarter-on-quarter changes I would expect, nothing more than that.

Anita Rangan: Sir, on a net basis how it would be the net NPL?

Management: Yes that is also more or less holding flat. Not much difference on a QOQ basis I am anticipating. And as far as HFC is concerned we are holding flat between 0.9% to 1% gross NPA so that the again fairly in line with the industry.

Anita Ranga: And with respect to the demerger just a follow up question from the previous one, how is the liability be transferred, will there be any kind of guarantees from the holdco for the commercial finance segment or how it would be like because I am assuming respect of the liabilities also would be relating to the CIC. So with say Reliance Capital's bonds or everything how would they be transferred?

Management: So, the High Court will come back on the entire scheme of arrangement and the entire bank borrowing would be moving down because bank borrowings are specifically for the commercial finance lending and so that is the bit which will move down a bit.

Anita Ranga: And the bond.

Management: The bond will primarily stay at the holdco. Some of them will go down because it will depend on the mix.

Anita Ranga: Okay but some portion of the bonds will be there in the CIC also.

Management: Absolutely, yes.

Anita Ranga: Okay.

Moderator: As there are no further questions I would now like to hand to hand the conference over to Mr. Asutosh Mishra for his closing comments.

Asutosh Mishra: Thanks everyone for participating in the call and management for giving their perspective on operating business. Thank you.

Moderator: Thank you members of the management team. Ladies and gentlemen on behalf of Reliance Securities that concludes this conference, thank you for joining us and you may now disconnect your lines.