Business Standard

Wed, 10 May-17; Business Standard - Mumbai; Size : 194 sq.cm.; Page : 12

Focus on core businesses to drive Reliance Capital's earnings

Value unlocking in key subsidiaries to keep sentiment positive on the stock

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Reliance Capital's (RCap's) focus on unlocking value of its subsidiaries and divesting non-core investments seems to have started bearing results. The RCap stock, which has seen significant erosion in its value - from over ₹2,900 in early 2008 to below ₹300 seen last year, has witnessed a sharp recovery in the past one year. Delivering 66 per cent since May 2016 and beating the benchmark BSE 100 index's 21 per cent gains in this period, the stock scaled to its six-year high last month-end.

There are quite a few reasons behind this surge, including the improving prospects of its general insurance business and continued traction in the asset management business. The company recently also got approval to demerge its housing finance subsidiary, Reliance Home Finance, which will be listed separately in a few months. Housing finance being seen as a high-potential industry has also helped push up sentiment. RCap has also demerged its commercial finance business; it now operates as a pure core investment company (CIC). In such a structure, it does not directly operate any business but holds majority stake in them.

Investors are also enthused by the company's plans to exit its private equity investments worth ₹2,000 crore as well as monetise its media and entertainment business. Such a move is seen positively as investment in these non-core businesses has compressed RCap's return ratios, even as it may have created value for the company. As RCap moves ahead on its plan to exit non-core businesses, its return on equity ratio is expected to improve from about 6.8 per cent in FY17 to 10 per cent in FY19.

SUM OF THE PARTS VALUATION

Business	₹ crore	₹/share
Asset management *	5,531	225
Life insurance *	3,568	145
Retail broking	645	26
Commercial finance	5,505	224
Home finance	2,599	106
General insurance	2,170	88
Investments	2,150	88
Fair value **		767

Data based on FY19 estimates
* for 51% stake each
**After holding company discount
Source: Edelweiss Securities

Meanwhile, the March 2017 quarter was also good. RCap continued to witness healthy traction in its asset management business even as improving profitability of the general insurance business aided overall earnings. While its commercial finance business also put up a decent show, the life insurance business reported another weak quarter.Its retail broking business — though a smaller part of the overall business — continues to witness high volatility and is likely to move in tandem with the trends in broader equity markets going forward, believe analysts.

In this backdrop, even as a CIC structure may warrant some holding company discount for RCap, most analysts are positive on stock. Their average target price of ₹744 apiece indicates an upside of nine per cent from current levels. Though a large part of potential gains from restructuring and value unlocking appear baked into current valuations, incremental newsflow around listing of home finance business and sale of investments will keep the stock buoyant.