Reliance Capital Limited
Q3 FY14 Earnings Conference Call
7th February 2014

SPEAKERS: Management of Reliance Capital

Moderator: Ladies and gentlemen good day and welcome to the Reliance Capital Q3 FY 2014, earnings conference call hosted by Axis Capital Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need any assistance during this conference call please signal an operator by pressing * and then 0 on your touchtone phone. Please note that this conference is being recorded. I now hand over the conference to Mr. Pravin Agarwal of Axis Capital. Thank you and over to you Sir.

Pravin Agarwal: Thank you, good evening everyone and welcome to this conference call. We have with us Mr. Sam Ghosh, CEO of Reliance Capital and other members of the senior management. At this point, I would like to hand over the call to Mr. Ghosh, who will brief us about the results and then we can start the Q&A. Over to you Sir.

Sam Ghosh: Thank you Pravin, and good evening to all of you and welcome to Q3 FY 2014 earnings conference call. We have the CEOs from our businesses with us, Mr. K. V. Srinivasan from commercial finance, Anup Rau from Life Insurance, Rakesh Jain from General Insurance, Vikrant Gugnani from Broking and Distribution Business; also we have Prateek Jain, CFO of Reliance Capital Asset Management as well as Reliance Capital's CFO Amit Bapna. First, let me present a brief summary of our consolidated Q3 results and an update on each of our businesses, after that we will take questions.

The total income from operations for the quarter increased by 10% to Rs. 19 billion while the consolidated net profit for the quarter rose by 65% to Rs. 2 billion. The net worth of Reliance Capital increased by 6% to Rs. 126 billion at the end of Q3 FY 2014. Despite challenging macro environment, we have improved the operating performance of our core businesses and will expect to continue to achieve profitable growth in each of them.

In Life Insurance, new business premium rose by 18% to Rs. 4 billion in this quarter driven by improved productivity by the agency force. In General Insurance, gross written premium increased by 21% to Rs. 6 billion. higher than the industry growth of 9%. In Commercial Finance, profit before tax rose by 24% to Rs. 1 billion driven by higher yields. We have improved our net interest margin to 5.6% in this quarter vis-à-vis 4.2% in Q3 FY 2013. In Asset Management, our mutual fund average assets under management crossed Rs. 1 trillion. We continue to maintain a market share of 12%. Profit before tax grew by 45% to Rs. 843 million driven by higher mutual fund AUM. We have given detailed financial 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 of the businesses.

Reliance Life Insurance continues to be among the leading private sector life insurance players with the private sector market share of 6%. The total premium for the quarter rose by 4% to Rs. 10 billion driven by an 18% increase in new business premium to Rs. 4 billion. 88% of the new individual business premium has been continued by traditional products. For the period ended December 31, 2013, Reliance Life Insurance maintained its position amongst the top 5 private sector insurance in terms of individual WRP. We have increased our average ticket size by 34% to over Rs. 20,400 in the quarter. We expect to continue with improvement in productivity as well as maintain our position amongst the top private sector insurance. Reliance Life Insurance sold over 150,000 individual policies in the quarter ended December 31, 2013 and was one of the highest in the private sector. Over 4 million individual life policies are in force as on December 31, 2013. Persistency has been stable at 53% for the quarter while agent persistency is over 60%. To improve this further, the business has taken several initiatives this year such as linking distributor and sales team compensation structure to persistency, conducting physical policy holder verification post issuance, focusing on higher ticket sizes and engaging prospective agents through the career distribution model. We expect to improve the third party distribution persistency following similar initiatives as in the agency model and further weeding out some partners. The profit before tax was Rs. 272 million. Also, further surplus arising from the nonparticipating business was at Rs. 743 million. The profits are lower than Q3 FY 2013 as the surrender charge income is declining. The declared results of Reliance Capital included consolidation of 48% stake in Reliance Life Insurance. The total funds under management rose to Rs. 181 billion as compared to Rs. 175 billion as on September 30, 2013. Reliance Life Insurance has a distribution network of over 900 offices across India.

Reliance General Insurance is amongst the top 5 private sector general insurance companies in India in terms of business premium with the private sector market share of 8%. The gross written premium for the quarter was Rs. 6 billion - an increase of 21%. The business made a profit of 241 million in Q3, but due to the one time negative impact of Rs. 135 million as a result of IRDA's recent advice for increase in provisioning for the motor declined this pool the profit stood at Rs. 106 million. The combined ratio rose to 125% for the quarter as against 112% in Q3 FY 2013 due to exceptional provisioning for the motor declined risk pool as stated earlier and third party motor claims reserving. Our focus on this business is to improve the combined ratio and to optimize the product portfolio towards the profitable mix.

Reliance Commercial Finance is amongst the leading lenders in the non-banking finance space. Our focus continues to be on secured asset lending to niche segments of mortgage, SME and commercial vehicle loans. The disbursement for the quarter rose by 5% to Rs. 24 billion. The assets under management grew by 3% to Rs. 164 billion. The outstanding loan book was at Rs. 137 billion. We securitized loans of over Rs. 2 billion during the quarter. Due to the challenging market conditions, the business has focused on improving NIM and controlling NPA rather than expanding the book. At the end of the quarter, 100% of the book continues to be secured. The total income for the quarter was higher by 5% at Rs. 6 billion while profit before tax increased by 24% to Rs. 1 billion driven by higher margins and stable opex ratios. Average yields in Q3 rose to 15.4% - an increase of over 110 basis points over the corresponding quarter last year. Net interest margins for the quarter were 5.6% as against 4.2% in Q3 FY 2013. The cost to income ratio improved to 16% for the quarter as against 16.5% in Q2 FY 2014. Gross NPA were at Rs. 4 billion, this translates to 2.4% of assets under management. The ratio has remained stable from September to December 2013. The coverage ratio including write offs at the end of December 2013 stood at 56% and excluding write offs the ratio was at 17%.

Reliance Capital Asset Management manages Rs. 1.9 trillion of assets across mutual fund, pension fund, managed accounts and offshore funds. Reliance Capital Asset Management is the largest asset manager in India. Reliance Mutual Fund is amongst the top 2 mutual fund in India with a market share of 12%. The average assets under management of Reliance Mutual Fund were at Rs. 1 trillion as at December 31, 2013 - an increase of 13%. We increased the share of retail debt to 36% of overall debt AUM as on December 31, 2013 as compared to 35% in December 2012. For the quarter ended December 31, 2013, the asset management business generated income of Rs. 2 billion. The business achieved a profit before tax of Rs. 843 million - an increase of 45% over the corresponding quarter last year driven by increase in mutual fund AUM. Reliance Mutual Fund continues to be amongst the most profitable mutual fund in India.

Reliance Securities is amongst the leading retail equity broking houses in India. The focus at Reliance Securities is on the key business verticals of equity and commodity broking and wealth management. In the broking vertical the equity broking accounts increased by 3% to over 727,000 and average daily equity turnover stood at Rs. 18 billion. The number of commodity broking accounts increased by 8% to over 41,800 and the daily average commodities turnover of Rs. 4 billion. In wealth management, assets under management stood at Rs. 12 billion - an increase of 33%. For the quarter the total income decreased by 17% to Rs. 524 million, while the business had a loss of Rs. 44 million due to fall in volumes in the equity as well as commodities segment.

Reliance Money is amongst the leading distributors of finance products and services in India with a distribution network of over 6,600 outlets. For the quarter, revenues were Rs. 357 million. The business made a loss of Rs. 28 million in the quarter due to lower income from distributor and third party products mutual funds and life insurance. The income is expected to increase in Q4 driven by higher insurance and mutual fund sale. Reliance Money is one of the largest private sector partners for Western Union Money Transfer in India and handled over 700,000 money transferred transactions during the quarter an increase of 17%.

In conclusion, I would like to say that all core businesses are on tracks in terms of operating performance and are expected to continue this trend of profitable growth on a consistent basis. Thank you very much. We can now take questions.

Moderator: Thank you very much sir. Participants we will now begin with the question and answer session. We have the first question from the line of Jai Mundhra from CRISIL Limited. Please go ahead.

Jai Mundhra: Sir, first few questions on your insurance business. Now this quarter APE is growing by 33%, so can you please throw some light on the growth now, I believe the regulatory changes are almost all done, how do you see the progress now onwards now in life insurance?

Company Speaker: I think it is a little too early to comment but then we are confident as far as growth is concerned, it will be sustained because I see it is not going to have an impact on distribution productivity. I do believe in the short-to-medium term, we could potentially lose some distribution as they will not able to match the increase in productivity to the commissions they were currently earning, because the commission structures are different but we are confident that our productivity will continue to go up and we will be able to replace any agent attrition with new hiring,

Jai Mundhra: Do you disclose the NBP margin or this is like annual or if you can give some ballpark number?

Company Speaker: It is given out annually.

Jai Mundhra: Sir the product mix is now undergoing a significant change year-on-year at least, the traditional products are now almost around 88%, of course this will continue right until and unless there is some thrust on ULIP again?

Company Speaker: Yes, we would want to maintain the traditional percentage of 80%.

Jai Mundhra: Sir a few clarifications on your presentation, what is this WRP in individual?

Company Speaker: Weighted premium which is basically the premium received on regular premium plus 10% weightage on single premium.

Jai Mundhra: Is this also for individual?

Company Speaker: Same for individual.

Jai Mundhra: Sir this market share you mentioned two places one is the market share which you mentioned in slide 8, is this for the quarter or cumulative APE market share, because they are two different numbers, one is 5.9 and one is 8% in nine months.

Company Speaker: YTD market share is about 8% and that is on new business premium basis, while 5.9% is for the quarter.

Jai Mundhra: Sir you are consolidating around 48% of life insurance in your consolidated results and if I look at your slide 28 which gives your consolidated financial this interest income of 9.5 billion this is interest income only on consumer finance or does this include life insurance?

Company Speaker: It does not include life insurance.

Jai Mundhra: So life insurance does not figure at all right in this revenue at least because you are consolidating only as a part of associate after PAT, what is this 9.5 billion then.

Company Speaker: This is interest income of commercial finance because commercial finance is part of capital itself plus home finance would be there, primarily these two businesses.

Moderator: We will take the next question from the line of Parag Jariwala from Macquarie Securities, please go ahead.

Parag Jariwala: Good evening sir. I have some questions on your consumer finance business. If you see in terms of CV loans, CV as a percentage of overall book is maintained at around 11 to 12% but if you see largely what is happening in CV industry currently ideally I think it should have come down drastically, so what is your view on overall situation in CV market and how you are able to grow this segment though in line with the industry?

Company Speaker: We have not reduced the share of commercial vehicles but what we have really done is we have changed the mix quite a lot. If you look at the market, the stress is more in the strategic segment the largest fleet operators whereas retail and the smaller vehicle loans are doing quite well, so about a year and a half ago we stopped doing much of this strategic business but moved considerably towards the LCV and small commercial vehicles and first time users, so basically we have gone totally retail, that is really helping us to maintain the book at the same time plus improve the net interest margin on this, what we have not done is to cut down the exposure but change the nature of the exposure significantly.

Parag Jariwala: Sir, what drives this margin expansion, not only this quarter but if you see since last one year it has gone up from 4.2 to 5.6 I understand that you borrow a large proportion from banks on lease but such kind of improvement in yields are very surprising?

Company Speaker: Basic thing is what I just said, we change the mix of the lending book considerably, so what we have done is that we have cut down on ticket size, go on more smaller towns, so on and so forth expanded our geography and obviously you would see from the report that the cost of funds itself has not changed much but the yields have increased significantly because of the mix change and that is precisely the main issue.

Parag Jariwala: Sir, in terms of NPA it has actually gone up by the end of FY 2013 it was 1.7, I agree that quarter-on-quarter it has not increased much but what is the outlook on this same going forward?

Company Speaker: I would expect this to be maintained at the same 2.3 kind of levels until the year end is over, now obviously the key factor is the ability to manage a few accounts because as I had mentioned earlier, a good part of the NPA is consisting of couple of larger loans, we don't have any kind of issue with the broad book per se but for a few cases which we are handling. We have full confidence that we will be able to recover the money and more.

Parag Jariwala: Is it possible for you to bifurcate this in terms of corporate and non corporate?

Company Speaker: We don't have corporate loans as part of the commercial finance business. Primarily, the lending is to the SME as well as the smaller businesses.

Parag Jariwala: Maybe retail and non-retail kind of?

Company Speaker: We don't have retail in that sense, we don't lend to consumers per se, so that is primarily 95% of our customer base is SME only, so it is all in one bucket but across products there could be small variations. The mortgage business will be little lower than the commercial vehicle business but that is the way things are but broadly, we don't have any consumer loans in the salaried segment at all.

Moderator: We have the next question from the line of Kajal Gandhi from ICICI Direct, please go ahead.

Kajal Gandhi: Good evening Sir, can you please share what is the reason for AMC reporting such strong profits?

Company Speaker: Obviously, if you see from the asset mix perspective, we have been working and we have had good retail debt over the last few quarters and that has started yielding results and it has been basically the change in the asset mix. We have not been working towards gathering the low yielding assets in terms of income or in terms of liquid fund and therefore our yield to AUM is higher and so is reflected in our earnings as well.

Kajal Gandhi: Are you saying we will consistently see this kind of number because this has not happened for several quarters?

Company Speaker: If you have seen quarter-on-quarter we have been working towards and as Sam also mentioned we are working towards the profitable growth, so we are not in the pursuit of only the topline, we will continuously grow profitably this year.

Kajal Gandhi: So we can expect such profitability and actually an improvement in profitability from the AMC business.

Company Speaker: Yes, we remain committed on the retail part of it which gives a better yield and also we will work on higher realizations.

Kajal Gandhi: Sir what is the MTM in this quarter in standalone?

Company Speaker: We have positive MTMs but there are no realized capital gains in these financial.

Kajal Gandhi: Sir on the loan book classification which we just talked about, are you going to share about the infra loans going forward or no?

Company Speaker: There is very little proportion of infra loans at this moment. We would wait for better times to come as far as this sector is concerned before we expand that, so we are on a wait and watch mode as far as the infra book is concerned.

Kajal Gandhi: Sir, on the life insurance side, is it that H2 profit is slightly not that great this time? Sir I just wanted to get a sense because Q3 should be slightly better than Q2 but it has been bad both on the premium side, is it that Q4 also is expected to be on the lower side?

Company Speaker: We have a surplus in the non-par business of about 74 Crores for Q3 as well which we have not booked, we can book it only after audit. We did the audit in H1, again after the end of the year, we will do an audit and the profit, the surplus in the non-par will be transferred again.

Kajal Gandhi: Now that there is lot more clarity that your subsidiaries profits are somewhat tallying to your consolidated reported PAT, what will be the trend going forward in terms of because in spite of the profit coming in your return ratios are not that great, so what will be the trend forward how are we looking there?

Company Speaker: If you look at it across the board, all our business is showing better profits and therefore they are linked to obviously the consolidated results also, so if they are showing better profits from our businesses that should reflect again in our consolidated results.

Kajal Gandhi: So, but then when do you expect to go to double digit on ROE side?

Company Speaker: If you look at our networth it is significantly high primarily because we have the life business capital gains in there, so I think going forward for us to achieve significant ROE will take time and in the meantime I think our focus now is to grow the profit year-on-year.

Moderator: We have the next question from the line of Ritesh Nambiar from UTI Mutual Fund, please go ahead.

Ritesh Nambiar: Good evening sir, just wanted color on the business climate, because again you have launched back to the quarterly disbursement rate of 2,400 that you had in Q4 and Q3 last year so a color from where this growth is coming and how we are able to achieve it?

Company Speaker: Primarily, we have not grown the book aggressively as a matter of conscious choice over the past five or six quarters now. I think, at least, until the economic situation clears up a bit and the capex demand picks up, I would expect that we would maintain this book more or less at the same level, may be some amount of growth, but the focus will always be therefore to maintain the book quality as well as the profitability, so I don't expect the situation to dramatically improve until the capex demand picks up which I would expect to take at least one or two quarters more.

Ritesh Nambiar: Sir, on the AMC business this Q4 generally is a good quarter for you, so where will the full year number be for the AMC?

Company Speaker: As mentioned, we will continue to grow profitably. We cannot give you forward looking statement but we will continue to do well in this business.

Ritesh Nambiar: But generally is it a lumpy Q4 or how is it actually?

Company Speaker: No, it will be consistent with what was there similar to last quarter.

Moderator: Thank you. We have the next question from the line of Nischint Chawate from Kotak Securities, please go ahead.

Nischint Chawathe: Did you book any capital gains during the quarter?

Company Speaker: No.

Nischint Chawathe: If I look at the provisioning number in the standalone balance sheet does this pertain purely to the NBFC business?

Company Speaker: It will be NBFC plus the corporate book.

Nischint Chawathe: How much from the corporate book would that be.

Company Speaker: That will be mostly from the NBFC book only.

Nischint Chawathe: Just some more data points, what could be the equity investment book as on the quarter end?

Company Speaker: It is similar to Q2 itself, the listed would be around 1,000 Crores. Nothing has significantly changed from Q2. The balance sheet remains similar.

Nischint Chawathe: Just trying to understand little bit about this open offer for Reliance Broadcast and what is the plan out here?

Company Speaker: There is an open offer where we would try and delist RBNL, so the group holds 70% plus currently and I think we will take it up to 90% and try and deal with this over the next month or two. The impact would be less than 100 Crores.

Nischint Chawathe: Incrementally, what is the thought process on making equity investment commitments over here because I guess you will need to invest now plus they are making losses and possibly need to support this one in the next couple of years?

Company Speaker: RBNL is EBITDA positive now and we will be looking at a partner coming in to this business at some point in time.

Nischint Chawathe: Basically at current stage you are looking at a billion rupees or so at this point in time?

Company Speaker: Yes, less than a billion rupees and we basically are looking for partners, and then we liquidate our holding.

Nischint Chawathe: Did you mention that the new business premium margin could kind of come down to around 15 odd percent next year, is that what you guided for?

Company Speaker: Yes the margins would come down to 15%; we do obviously expect to enhance productivity.

Moderator: Next question from the line of Sanket Godha from JM Financial, please go ahead.

Sanket Godha: My question is with respect to life insurance, just wanted to know the product mix within traditional how much is par and non par because I understand these compositions will impact the margins and change in this mix has majorly lead to decline in margins from 20 to 15.

Company Speaker: I think the margins have declined on account of the new regulations on traditional products. If you are talking about the mix, 50% of the traditional mix would be par, 50% would be non par. We do expect to take the non par mix to higher

Sanket Godha: Just wanted to know, all the new products have been launched like whatever we have planned and we are with full suite of products with January 1?

Company Speaker: Yes we have, we have started selling all new products on January 1.

Sanket Godha: So the growth which we have achieved in nine months, is that sustainable going ahead or would taper down a bit?

Company Speaker: We believe we will be able to sustain the growth. In the short term, we expect some challenges with some distributors exiting, but we feel that with focused improvement on productivity which we have already witnessed throughout the year and also the increase in the number of people who are working with us, we should be able to mitigate these challenges.

Sanket Godha: Just wanted to understand the sense of new products, how it has been in the month of January, the off-take of the new products, the growth that you have got in the month of last quarter, Q3, is it on similar lines or is it a little lower?

Anup Rau: I think the product morale is unchanged. I think one of the focus areas for us over the last few months has been to increase the tenure of the policy and we have been getting traditional for a long time. From a customer perspective, really nothing changes, the only proposition that changes is for the distribution, so I don't see a problem on the demand side. It is not going to worsen or get better with the same products.

Sanket Godha: For the longer tenure products the commission structure is broadly the same, as you are focusing on the long term products the growth will not be much, is that the point you are trying to say?

Anup Rau: I think there are two points I am going to make here. One is obviously, in case, you sell a longer product, the proposition with the customer is better because insurance as a product if the customer is to make reasonable returns we would expect the customer to stay invested for a longer period of time and get protection for a period of time. As far as distributors are concerned, their compensation depends on the tenor of the product. So, I think that idea is somewhere to make sure that the customer get the right proposition and the distributors also are able to get income through selling longer tenor policies and the larger premium amount month on month. As far as being able to balance these objectives or meet both these objectives, I don't see a problem in retaining distribution, and customer proposition is only getting better, it is not worsening with new product launch, so our experience for the mix has been the same for the month of January.

Sanket Godha: Can I get the agency force strength right now, current agency force strength?

Company Speaker: We do have a reset every quarter in terms of the agent number, so currently it is in the ballpark region of about one lakh.

Sanket Godha: So for FY 2014 also we can assume a growth of say 15-20% for the company?

Company Speaker: I think we will have double digit growth and we will outperform the market, so that is something that we will do better than the street and the market.

Sanket Godha: One last question I know you guys don't disclose on cost overruns, but just wanted to understand how it is right now, whether the company is under the control of cost overruns and how is it actually?

Company Speaker: In case if you want to look at our expenses on an absolute I think we run a very efficient organization in terms of absolute opex we are among the leanest operators in the industry, in fact if you look at our branch operating cost, it amounts to lowest in the industry, so we run a very efficient ship. We do believe that the upside is going to come through productivity and that is what we are going to be focused on, so yes we don't disclose overruns but just to give you a flavor of what we are planning to do, we plan to improve productivity that is going to be our strategy.

Moderator: We have the next question from the line of Manish Shukla from Deutsche Bank, please go ahead.

Manish Shukla: On general insurance, first could you quantify the extent of motor pool provision which is leading to the increase in combined ratio for the last two quarters September and December?

Rakesh Jain: I think the motor pool this quarter we have taken about 34 Crores which was not there in the corresponding quarter last year.

Manish Shukla: September quarter what could this have been?

Rakesh Jain: September quarter on a running basis was about 20 Crores.

Manish Shukla: Because September quarter also, we saw about 700 basis points deterioration in combined ratio from 113 to 120.

Rakesh Jain: There are two parts to the provision, one of course, was the motor pool and then there had been certain interest accruals. If you see our investment income and the claims, and if you see yield, there is almost 46 Crores which is accrued on the investment income on account of claims in this quarter and the same amount has also got added over and above the 34, which I have said in the claims incurred. Now the way we calculate the combined ratio actually we don't take the credit of what accrues to the investment income so it is before that.

Manish Shukla: What is the balance remaining on this?

Rakesh Jain: About 20 Crores for the last quarter which will end everything hopefully.

Manish Shukla: Nothing spilling over to next year right?

Rakesh Jain: No.

Manish Shukla: On commercial finance, could I get the borrowing mix across instruments, bank loans, CP, NCDS.

Company Speaker: I think substantial part of it would be through bank loans, Amit do you have the exact numbers?

Amit Bapna: Yes, roughly 75% plus would be bank loans for the commercial finance business and balance would be CPs and NCDs.

Manish Shukla: Right and I think this was discussed a bit earlier but just want to check again, on year-on-year basis on commercial finance, there is a very sharp jump in asset yields, I could not quite understand why that jump is coming through, it is almost 120 basis points the increase in December 2013 versus December 2012.

Company Speaker: The change as I mentioned is essentially coming in because of the change in product mix. Now what we have done is that we have cut down the average ticket sizes and gone more to the smaller ticket size where our yields are significantly better and certain areas, like for instance, we have completely cut down the car loan business which was a low yielding business, so what you see in the composite interest rate is only a reducing part of the car loan business which will eventually run out and on the commercial vehicles itself we took a call about a year, year and a half ago to cut down on the strategic segment and go more retail where the yields are significantly more and similarly is the case with your SME business, so that has exactly what has changed the interest margins.

Moderator: Participants that was the last question, I now hand over the floor to Mr. Sam Ghosh for closing comments. Thank you and over to you Sir.

Sam Ghosh: Thank you. I think this quarter has been very good for the company in that profits have grown significantly. Next quarter, we expect all our businesses to outperform what they have achieved in this quarter. So with those words, I think this company has performed the way we were expecting it to, each of the businesses have turned out doing a good job and we expect it to continue for the last quarter. Thank you very much.

Moderator: Thank you Sir, ladies and gentlemen, on behalf of Axis Capital, that concludes this conference call, thank you for joining us you may now disconnect your lines.