Religare Enterprises Limited

Q3 FY13 Earnings Conference Call

Tuesday, January 29, 2013 at 03:30 pm IST

Kishore Belai : Good afternoon everyone and thank you for joining us on our Third Quarter FY13 results conference call. I am Kishore Belai, Head of Investor Relations at Religare. We are joined on this call today by Mr. Shachindra Nath, our Group CEO and the senior management of our portfolio companies. Before we start the proceedings, I'd like to mention that certain statements that may be made on this call may be forward-looking statements and we do not undertake to publicly update them. A statement in this regard has been included in the invitation for this call.

On this call, Mr. Nath will first give you an update on the performance of the portfolio companies through the quarter. We will subsequently open the lines for Q&A. I now turn the call over to Mr. Nath.

Shachindra Nath : Thank you Kishore. Good afternoon everybody and thank you for joining us on this call. I hope you have been able to study our results presentation which has been uploaded on our website and emailed to you as well.

Let me first talk about how some of the key economic indicators shaped up in Q3FY13. As you can see on pages 2 and 3 of our results presentation, the Capital Market was supported by FII inflows during the quarter but the other indicators have not instilled any confidence in the outlook.

GDP growth stood at 5.3% in Q2FY13, a multi-year low signalling a further slowdown in economic activity. The Reserve Bank of India has reduced its GDP growth forecast twice in this financial year, from 6.5% at the start of the year to 5.8% and further to 5.5% yesterday. While the RBI kept the Repo rate unchanged at 8% for nine months, they have finally relented to the demands of industry and the Government, and reduced the rate by 25 basis points, supplemented by a 25 basis point cut in the Cash Reserve Ratio at today's Quarterly Monetary Policy Review.

The Equity Markets have been a bit of a bright spot during Q3. The momentum in FII inflows seen during Q2FY13 continued into Q3FY13 and the Indian market received ₹460 billion in net FII inflows.

In fact, this momentum has continued into the current quarter as well and in the first four weeks of January, India witnessed a total inflow of ₹190 billion or nearly USD 3.5 billion. Our Capital Markets business interacts with various global investors on a daily basis and this interaction suggests that there is a lot more positivity in the international investor community about India although domestic investors have been exiting the market. Equity market volumes moved in tandem with FII inflows and we saw total volumes of ₹105 trillion in Q3FY13, the fourth straight quarter of increase in volumes. In terms of composition of volumes, the share of the Cash segment increased marginally to 8%, while share of Options remained unchanged at 76%.

Mutual Fund Industry AUM increased to ₹7.6 trillion and inflows remain concentrated in Liquid Funds and Debt Funds.

M&A and ECM deal volumes jumped significantly during the quarter to around USD 10 billion on the back of some large IPOs. However, the lacklustre post-IPO performance has deflated the initial hope of a revival in retail participation in the market.

In the Life Insurance industry, New Business Premium in October and November 2012 was essentially flat year-on-year.

In summary, the Capital Market is showing signs of life but the real economy is lagging. While this lead-lag is a normal phenomenon, we think it's a bit early to call a full revival.

Let me now give you a brief update on each of our portfolio companies, which is summarised on slides 4 to 6 of the presentation. In **Religare Securities Limited** and **Religare Commodities Limited**, our Retail Broking business, the efforts towards operational improvements are yielding results as the business returned to profitability in Q3. Market share is steady both in equities and commodities. Our distribution metrics remain robust with equities client base standing at 838,000 and commodities client base standing at 169,000 as on 31st December 2012.

Our retail broking business reported steady revenue quarter-on-quarter at ₹1,064 million. More importantly, we have turned the business around, and from a negative PBT of ₹56 million in Q2, it delivered a positive PBT of ₹37 million in Q3. It has taken an exceptional amount of hard work to achieve this turnaround, and we believe that the most difficult phase is behind us. We are quite confident that this business will continue to improve its performance and deliver to its full potential in the near future.

Religare Asset Management Company Limited, which operates our India Asset Management business, recorded an 11% QOQ increase in AUM which is better than industry growth of 5% QOQ. The business witnessed inflows from retail investors in long duration debt funds during the quarter, in anticipation of the interest rate softening cycle getting kick-started. On the last call, I had talked to you about the proposed acquisition of equity stake by Invesco in RAMC. We have completed all formalities on our part and are awaiting regulatory approval for closing the transaction.

In **Religare Macquarie Wealth Management Limited**, our Wealth Management Joint Venture, our AUM stood at ₹28.8 billion as at 31st December 2012, with consistent improvement in Relationship Manager-productivity. With the platform stabilising and costs at sustainable levels, we have undertaken some new initiatives to expand the product proposition and drive future revenue.

Religare Finvest Limited, which houses our Lending Business, is following a cautious approach in the current uncertain environment. As a result, the loan book stood at ₹108.2 billion as at 31st December 2012, lower versus the previous quarter. The Core NIM was at 3.91% which is within our target band. Reported net NPAs on 90 days basis stood at 0.97%, higher QOQ by 16 basis points due to a lower book size and reflecting seasoning of the portfolio. On a 180-day basis, which is the norm prescribed by RBI, both Gross and Net NPAs were significantly lower and relatively steady QOQ. RFL's CRAR stood at 20.05% at the end of the quarter, reflecting a good capital cushion for the expansion of business. RFL has adopted a risk-averse approach as it is continuously monitoring the evolving environment very closely and is focused on strengthening the balance sheet and improving operating parameters.

Religare Health Insurance Company Limited, our Health Insurance venture, continues to expand its distribution and coverage. It is now present in 28 cities through a network of 32 branches covering 124 locations. RHICL has enrolled more than 1700 hospitals in over 260 cities in its cashless provider network. The business generated Gross Written Premium of ₹93.4 million in Q3FY13 and provides health cover to more than 89,000 lives as on 31st December 2012. Cumulative Gross Written Premium collection since commencement of operations in July 2012 is now ₹197.8 million. Capital position is comfortable with solvency position at 284% as on 31st December 2012.

AEGON Religare Life Insurance Company Limited, our Life Insurance JV, continues to build its franchise with an increase in the customer base to 251,000 customers from 240,000 with around 12,800 policies issued in this quarter. The business is focussing its efforts on mining its customer base for repeat business and use of nonconventional distribution channels, specifically the online channel, in which we enjoy a pre-eminent position.

Religare Capital Markets Limited continues to focus on sustainability of the platform and accelerating the path to profitability. As at 31st December 2012, the business was empanelled with 604 institutional investors globally with active coverage of 250 stocks out of which India research now covers 149 stocks. RCML Singapore maintained its 2nd rank by number of deals and 11th rank by deal volume out of 23 banks for Singapore equity offerings, as per Bloomberg. We have seen some traction in ECM in Asia and during the quarter, we had our best ever revenue performance in the Asia Institutional Equities business. As you know, we do not consolidate the financial statements of RCML with REL since 1st October 2011, but the business continues to remain operationally integrated with the rest of Religare.

Let me now give you an overview of the consolidated financials of Religare Enterprises, which you will find on slides 7 to 9.

Revenue for Q3 was up 11% YOY to ₹8,662 million. We reported Profit Before Tax of ₹568 million for Q3FY13, reflecting YOY growth of 6%, but lower than the previous quarter's ₹1,009 million. Profit After Tax for Q3FY13 was ₹195 million as against ₹500 million in Q2 lower by ₹305 million QOQ on account of the following :

- PAT in Religare Finvest was lower by ₹243 million due to lower book size and higher provisions.
- Loss in Religare Health Insurance was higher by ₹26 million as the operations are being scaled up.
- Net negative impact from other operating companies was ₹57 million.
- Net negative Impact from Religare Enterprises Limited at the standalone level was ₹74 million, largely on account of interest expense on IFC CCDs.
- The above negatives were partially offset by an improvement of ₹95 million in Retail Broking.

To conclude, our performance during the quarter reflects the movement in the macro variables Capital Market-related businesses have done somewhat better while the businesses that directly address the real sector have faced some headwinds. In fact, this is a great validation of the diversified business model that we have adopted at Religare. We continue to be watchful as we believe that it is still early to call a revival in the economy.

With that, I come to the end of my opening remarks. The senior management of REL, our portfolio companies and I would be glad to address any queries that you may have.

Moderator : We have the first question from Nischint Chawathe of Kotak Securities. Please go ahead.

Nischint Chawathe : Three questions from my side. First is on Religare Finvest**.** If you could give us some outlook as to what you really see in this business because the broking book has been declining for last 2 quarters and so are the earnings. We have still not seen anything on the NPL side but what is the view out there on growth and asset quality?

The other pertains to Religare AMC. We have seen a sharp rise in the operating expenses on a quarter-on-quarter basis. Can you help us understand what is happening out here?

Finally the third question on the wealth management business. What would be the optimum level of AuMs per RM and you think this is a good time to break even?

Shachindra Nath : Kavi would answer your question respect to Finvest and Saurabh can take asset management and we will take wealth management.

Kavi Arora : We have said in the last two quarters that the macro environment being the way it is, we will have a slightly cautious approach on growing our credit portfolio in these times and that's what is clearly reflecting in our new acquisition volumes for the last 2 quarters. Having said that, we continue to maintain a little hawkish view on how the macro environment is changing. Fundamentally not much has changed. There will be a marginal increase in the AUM by the end of the year that is this quarter. We will grow the portfolio from where it is as of 31st December.

On the performance of the book, as Shachin mentioned in his opening remarks as well, there is a very marginal increase because of seasoning and our portfolio decline is of about around ₹ 300 crore in the last quarter. And thus if you look at on 180 days basis, it is the norm or net NPAs are sub 0.5% or 0.47% to be precise. If you look at the capital adequacy ratio at 20%, it indicates that the moment we start seeing the environment getting a little better, we can start growing the book a little more aggressively compared to what we are doing today.

One of the segments which we have really slowed down on acquisition is the construction equipment and commercial vehicle segment where everybody else is also cautious and that is clearly reflecting in the new acquisition volume in those businesses.

Nischint Chawathe : Anything to read in the quarter-on-quarter rise in operating expenses in RFL?

Kavi Arora : In RFL the actual operating expenses have stayed where they are if you look at both personnel and there are only couple of extra ordinary items which all got clubbed in operating and administrative expenses. If you look at it, the number is the same and our OPEX to ANR which was 1.76% in last quarter is 1.80% this quarter which is purely on account of decline in book by ₹300 crore. On basic business operating expense, there is actually no increase.

Saurabh Nanavati : The total income has also gone up by an equivalent amount as compared with the operating and administrative expenses. The biggest reason is the change in regulations effective 1st October where the exit loads will now start getting credited back to the NAV of the scheme and in turn the AMCs have been allowed to charge 20 basis points of additional fees. So to that extent, the total income has gone up but the expenses will also move up because the marketing expenses we incur, will be from the balance sheet and we cannot use the exit loads which were allowed earlier by the regulator.

Secondly, we also had an initial offer period for one of our funds Religare Bank Debt Fund which collected ₹115 crore in the month of December and there were upfront commissions paid out in that. This was also booked in the month of December. I think those were the two big reasons why the operating and administrative expenses have gone up.

Shachindra Nath ; With respect to your last question I would like to mention that the business is very close to break even. The operational gap is very low now and it is not directly linked to the Asset under Management. As you know, AUM does not flow into our P&L as a fee income necessarily. And it is more related to the productivity of relationship managers and what new product offering you can offer to your customers. So depending upon in which market cycle, how equity market is doing and what new products you can bring to your customers, you can breakeven with the same amount of AUM. We constantly keep working on improving the productivity of the clients and also on-boarding new clients with healthy AUM but we do not target asset under management to reflect breakeven of the business.

Moderator : Our next question is from Pankaj Agarwal from Ambit Capital. Please go ahead.

Pankaj Agarwal : If I look at your brokerage income it is flat on QoQ basis but if I look at cash market volumes during the quarter they are up 10% sequentially. So why there is a disconnect? Have the yields fallen during quarter-on-quarter?

Jayant Manglik : If you look at the market, it also consists of institutional equity's volume as well perse if you look at our brokerage volume, it is purely retail brokerage.. There is no peer comparison that you can make between broking and institutional volumes. Hence, you cannot directly translate the market volume to a retail brokerage outfit because for retail brokerage outfit, you have to compare it with the retail market volume. So your exchange volumes may not directly reflect the retail brokerage volume.

Pankaj Agarwal : It would be fair to say that the increase in cash market volumes have come from institutional segment rather retail segments in this quarter?

Jayant Manglik : That is true. Everyone is well aware that most of the volume, which you are seeing in the market are happening because of the FII inflows. Retail volumes are not yet back to the market.

Basab Mitra : If you just look at the slide on page 13 you can see the market share has been held steady. Where again it is the reflection of the fact that most of the volume growth in cash has happened from the institutional segment.

Pankaj Agarwal : Coming to your lending business, I am seeing your loan portfolio is de-growing over last 2-3 quarters in most of the segments. Any particular reason for being conservative in this environment?

Kavi Arora : One of the product lines is construction equipment and commercial vehicles. We continue to maintain a very hawkish view because of decline in average rentals, increase in input cost, the whole profitability in the segment is little challenged. When you look at construction equipment and mining equipment, because of slowdown in infrastructure and mining activity, there is a lot of stress on the assets in the market. We stopped as we are looking at this business since January of last year. So that is a reason for adopting a hawkish view and a little cautious view. We have a significant size in the market and the market environment remains challenging. We are not acquiring as many assets as we were acquiring in the past though our existing portfolio continues to perform reasonably well. Thus with the repayments we were seeing net decline in AUM for last two quarters only. And as I said earlier as well, if the market improves, we have enough cushion from capital adequacy point of view and the relationship that we enjoy with the banks for our debt lines. We can start growing AUM which could be positive from here on.

Pankaj Agarwal : But your loan book even in loan against property has come down which I believe is a segment that is still doing quite well as I hear from other lenders.

Kavi Arora : It has come down from our book perspective because the acquisition is slower compared to the natural run down in the book that happens from month- to month or quarter to quarter. There is a very marginal decline in that book.

Pankaj Agarwal : Is it because of lower opportunities or more competition in this segment i.e loan against property?

Kavi Arora : It is slightly more because of tighter credit view and tighter view on the incoming volumes on credit primarily.

Pankaj Agarwal : In terms of asset quality, you believe that loan against property is doing quite well?

Kavi Arora : Absolutely.

Moderator : Our next question is from Ritesh Nambiar of UTI Mutual Fund. Please go ahead.

Ritesh Nambiar : Given the latest guidelines on risk weights on capital market exposure, would you grow this book? Whether the book will be stable around ₹2000 odd crore levels or you are going to completely stop being aggressive in this book? Any take on that?

Kavi Arora : As any business decision is largely related to the kind of returns it generates. It is a real ROE equation in any business that determines whether we will grow or we will stay or we will exit in a particular business segment. Having said that with the risk weight changing, which is not implemented yet but if it gets implemented in the next financial year, you will have to look at how the market responds to increase in pricing because of risk weight going to 150%. And largely on a capital market lending side, we said it has its own limited opportunity in terms of growing the book to a certain size. As of now we see this around the levels that we are at around ₹2000 crore.

Shachindra Nath : We have always maintained that our capital market finance book and portfolio would continue to remain flat irrespective of the size of the total asset base of the company because we do not intend to grow our capital market financing in proportion to our asset finance business. So it would continue to remain flat whether it would come down from its current level or not, we will see how pricing get impacted post the new risk weights getting implemented on NBFCs.

Ritesh Nambiar : Some colour on disbursements if you could provide. How is the movement being, how is the growth being, gross disbursements?

Kavi Arora : From average disbursements in a quarter from about levels of ₹1200 to ₹1500 crore, in the last couple of quarters, we are nearly ₹400 or 300 crore. We see nearly ₹800 to 1000 crore disbursement in next few quarters.

Moderator : Our next question is from Chandan Gehlot of Deutsche Asset Management. Please go ahead.

Chandan Gehlot : Wanted to know the 90 days DPD has grown from 1.03% to 1.96%. Wanted to get a sense, is this coming from a particular account or it is coming from multiple accounts?

Kavi Arora : It's a combination of both. We have discussed in last couple of calls that one large account has been declared NPA. It also reflects that one large account moving as NPA plus with the overall seasoning of the book, we will see a bit of increase in our gross NPA numbers as identified at 90 days. And that's what is clearly reflecting.

Chandan Gehlot : What is your outlook going forward in terms of asset quality. Do you think asset quality is going to worsen further or we have already peaked?

Kavi Arora : We have said it will be stable and near peak and we see trends to continue at these levels, and with resolutions in few accounts rather start to look down.

Chandan Gehlot : What are the remedial steps that have been taken from management side to recover these dues?

Kavi Arora : I think it is regular business practice that continues. I do not think there is any change in the way we operate. The normal legal collection and legal recourse on the delinquent accounts continues to be pursued.

Chandan Gehlot : How is the capital market book performing? Do you see any further pressure on this book?

Kavi Arora : Book has been fairly stable in terms of performance and purely in terms of the returns and profitability, as we have said, we will maintain capital market books at the levels that they are which is around ₹2000 crore. It has nothing to do with the performance. It is a larger view that what percentage of the business do we see coming from capital market business. Performance wise pretty it is stable.

Moderator : Our next question is from Ravi Mittal of BNP Paribas. Please go ahead.

Ravi Mittal : Could you share the number of provision and write off for Religare Finvest for this particular quarter? And second, there was one media release regarding a proposed sale of lease portfolio by Religare Finvest to Magma Fincorp. If you can throw some light on that, that would be grateful.

Kavi Arora : One of the things that we have very actively pursued is to focus on the risk segments that we are building our competencies on and we have clearly defined SME as the segment where we are going to operate. We are looking at rebalancing some of the asset portfolios to align to our larger strategy on strengthening our overall SME credit machineries. In auto lease, which is largely a corporate risk, corporate credit under writing; it was not making any strategic sense to keep in our own overall book. So we have signed an agreement to sell this book of about ₹ 250 crore to Magma. We have got our approval from CCI. Over next few weeks, we should be able to execute this sale.

Ravi Mittal : And on the provision write-off number?

Kavi Arora : Year-to-date credit cost number is ₹93 crore.

Ravi Mittal : That means for the 9 months, right?

Kavi Arora : Yes.

Moderator : We have the next question from Vikas Garg from L&T Mutual Fund. Please go ahead.

Vikas Garg : I was not able to understand the breakup of RFL's inventory book which is of ₹500 crore plus. If I recall from my earlier discussions, you used to run book on the gold commodity trading as well. So just to take your sense, would there be any kind of impact post the increase in the import duty? Other than the gold commodity book, what kind of a book are you running in the inventory side?

Sunil Garg : Inventory in Religare Finvest comprises of some short term investments which we have done in bonds. As you know we are into arbitrage activity. One leg is where we invest into shares and if it is lying on a particular day it forms part of the inventory. All those are part of bonds or shares which are a part of our short term investments that's lying as inventory.

Shachindra Nath : But just to clarify, we do not need any proprietary equity position per se. They are part of our treasury management and arbitrage which is one side of the book, which is in cash segment. Those positions get reflected as inventory in our books.

Vikas Garg : Out of ₹ 500 odd crore, how much would be in the equity arbitrage?

Sunil Garg : Overall equity arbitrage at any given point of time is in the range of ₹200 crore. Partly it would be into cash arbitrage and partly it would be in F&O.

Vikas Garg : On the corporate bond side, mostly would these be all liquid names?

Sunil Garg : These are all liquid bonds. Bonds of PSUs and good quality corporates. These are what we are holding.

Moderator : We will take the next question from Devesh Dokwal from Reliance Mutual Fund. Please go ahead.

Devesh Dokwal : In Religare Finvest, all asset classes have seen a decline in AUM. But the corporate loan book has grown in the last couple of quarters. So what is the strategy here and what could be the number say at March '13?

Kavi Arora : The corporate loan book has also stayed where it is, it has not really grown. And as we said, I have explained the other view, which is given where the environment is and given the challenges that we have seen in the market, we controlled our new acquisition to a certain level and we raised a bar on the incoming credit in our book. And that is the reason for a little bit of decline in the book just in last two quarters. With the outlook getting a little more positive we will start growing again as we have enough cushion both on equity and debt size to grow the book. And we have distribution already in place. The corporate loan book is also at same level where it is.

Devesh Dokwal : Should we expect this number to stay at around these levels or we will see a decline or a growth?

Kavi Arora : One other thing which I had mentioned in response to a question a little while ago that we are continuously rebalancing our assets portfolio to align it more to Religare Finvest's long term strategy of building expertise in the SME space and building our book around SME credits in the market. As part of the rebalancing exercise we already moved out or sold our auto lease business which is not strategic. Even corporate loan book is not strategic to our growth from our future perspective. We will actually see a decline in this book.

Devesh Dokwal : These will be largely secured loans or unsecured loans?

Kavi Arora : Combination of both but very largely secured.

Moderator : There are no further questions at this time.

Shachindra Nath : Thank you for attending this call. If you have any more queries, please feel free to contact Kishore Belai, our Head of Investor Relations – he will be happy to be of assistance. Have a great day ahead. Thank you.

Note: *This transcript has been edited to improve readability*