Reliance Capital

Financial powerhouse

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Reliance Capital

STOCK INFO.	BLOOMBERG
BSE Sensex: 15,319	RCFT.IN
	REUTERS CODE
S&P CNX: 4,464	RLCP.BO

31 August 2007 **Buy**

Initiating Coverage Rs1,200

Y/E MARCH	2006	2007	2008E	2009E
Revenue (Rs b)	9.5	21.6	35.0	52.2
EBITDA (Rs b)	6.8	8.4	12.7	18.8
NP (Rs b)	5.8	7.0	9.1	12.6
EPS (Rs)	25.6	28.6	37.1	51.0
EPS Growth (%)	-	11.7	29.8	37.5
BV/Share (Rs)	188.5	215.4	248.0	293.2
P/E (x)	46.9	42.0	32.3	23.5
P/BV (x)	6.4	5.6	4.8	4.1
RoE (%)	-	14.8	16.0	18.8
RoA (%)	-	12.6	10.4	8.9

KEY FINANCIALS	
Shares Outstanding (m)	246.2
Market Cap. (Rs b)	295.3
Market Cap. (US$b)	7.2
Past 3 yrs EBITDA Growth (%)	N.A.
Past 3 yrs NP Growth (%)	N.A.
Dividend Payout (%)	12.3
Dividend Yield (%)	0.3
P/E to Growth (x)	0.9

STOCK DATA	
52-W High/Low Range (Rs)	1,302/462
Major Shareholders (as of June 2007)	(%)
Promoters	52.5
Domestic Institutions	2.6
Foreign	30.7
Public	14.2
Average Daily Turnover	
Volume ('000 shares)	2,312.4
Value (Rs million)	1,794.1
1/6/12 Month Rel. Performance (%)	1/73/127
1/6/12 Month Abs. Performance (%)	0/90/158

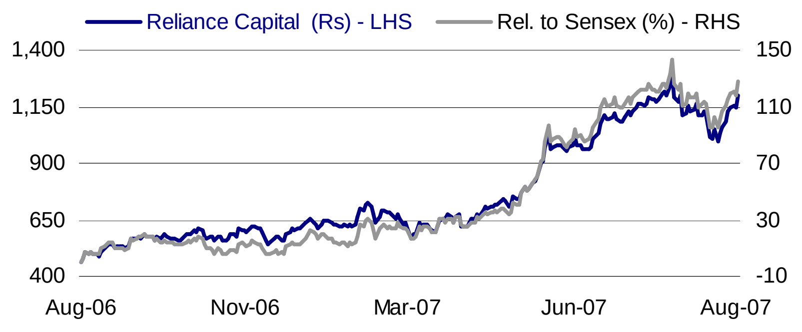
Emerging as a financial powerhouse: Reliance Capital (RCFT) is all set to emerge as a financial powerhouse in India with all its businesses - asset management, insurance, broking & distribution, and financing - outpacing sector growth rates. We expect exponential growth in the Indian financial services industry on the back of favorable macro economic dynamics. RCFT, with its strong management and well capitalized balance sheet, is likely to be a major beneficiary.

Vying for market leadership across businesses: RCFT is the largest player in the asset management business in India and is targeting market leadership across most other businesses like life insurance and brokerage. We expect RCFT to emerge as a key player in most of its businesses on the back of rapid branch network expansion, manpower addition, and intensive cross-selling among Reliance ADAG customers.

Insurance - a key value driver: Within a period of less than two years, RCFT has emerged as the fastest growing insurance company. Reliance Life is now the sixth largest private player in India based on annualized first year premium (APE), while Reliance General Insurance is the third largest private player based on gross premium written YTD July 2007. The management aims to be among the top-3 players in the insurance business in the next two years. We believe insurance valuation would be a key driver for the stock going forward, as RCFT owns 100% of its life and non-life insurance ventures.

Creating scale across businesses; Buy: We expect huge value accretion, as RCFT's new businesses (insurance, NBFC, and broking & distribution) attain scale. Our SOTP-based price target is Rs1,574 per share, an upside of 31%. We initiate coverage with a **Buy.**

STOCK PERFORMANCE (1 YEAR)



Reliance Capital
(Rs55b of Net Worth - 1QFY08)

Amitabh Chaturvedi, Group President - CA with over 18 years experience in banking & finance
Ex-MD and CEO of ICICI Direct.com and
Ex-CEO of Reliance Asset Management Co.

Asset Management

- 100% owned by RCap
- Largest MF in India
- Aims at maintaining leadership and growing retail customer base

Vikrant Gugnani, CEO - CA by profession and ex-Citibanker, has experience of managing a multitude of functions including financial management, project development and implementation related to investments, retail banking, and manufacturing

Life Insurance

- 16% direct stake, 100% economic stake through associate companies
- Sixth largest private player currently
- Aims to be among top-3 private players in next two years

P Nandgopal, CEO - Over two decades of experience in financial services industry

General Insurance

- 100% owned by RCap
- Third largest private player
- Aims to be among top-2 players over next two years

K A Soma Sekharan, CEO - 33 years of general insurance experience

Broking & Distribution

- 100% owned through associates
- Launched in April 2007
- Customer base exceeds 0.1m and network of 4,000 outlets in June 2007

Sudip Bandopadhyay, CEO - Ex Head of Treasury and Investments at ITC group

Consumer & SME Finance

- Conducted though RCap
- Selectively launched in four metros in 1QFY08
- Would leverage on net worth of RCap to fast grow the loan book

Amitabh Chaturvedi, Group President

Other Businesses

Asset Reconstruction Company - 49% held by RCap, 30% by banks and FIs and rest with FIIs

Rajendra Kakkar, CEO - First MD & CEO of Arcil, the first ARC in the country
Undertook the crucial task of setting up Arcil

Initiating coverage with a Buy rating

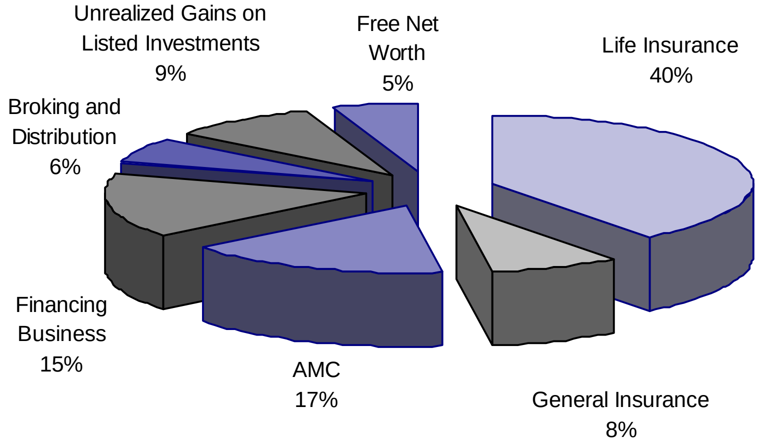
We believe RCFT is all set to emerge as a financial powerhouse in India. We expect huge value accretion, as its new businesses (insurance, NBFC, and broking & distribution) attain scale. We have valued the business on SOTP basis to arrive at a price target of Rs1,574 per share, an upside of 31% from current levels. We initiate coverage with a **Buy.**

VALUATION OF RELIANCE CAPITAL

	(RS B)	US$B	VALUE PER SH. RS	% TO TOTAL	RATIONALE
Asset Management	63.9	1.6	259	16.5	MF Market share of 16% in FY09E, Total AUMs to grow at 45% CAGR in FY07-09E, Valued at 6% of AUM FY09E
Life Insurance Business	153.7	3.8	624	39.7	Valued at 20xFY09E NBAP, 143% APE CAGR FY07-09E, 18% NBAP margins
General Insurance Business	31.0	0.8	126	8.0	Normalized operating profit margin of 3% of NWP, Valued at 20x FY09E normalised profits
Broking and Distribution	23.5	0.6	95	6.1	PAT margin of 30% in FY10, Valued at 15x FY10E PAT - discounted to FY09 @15%
Financing Business	59.6	1.5	242	15.4	Total equity funds of Rs18b, 3x leverage in FY09, Valued at 2.5x FY09E BV
Unrealized gains on listed investments	35.2	0.9	143	9.1	Actual as of 31 August 2007
Valuation of free networth	20.5	0.5	83	5.3	2x book value
Total Value	**387.4**	**9.5**	**1,574**	**100**	
Current Marke Value	**295.3**	**7.2**	**1,200**		
Potential Upside (%)	*31*				

Source: Motilal Oswal Securities

RELIANCE CAP: TOTAL VALUE RS387B



Source: Company/Motilal Oswal Securities

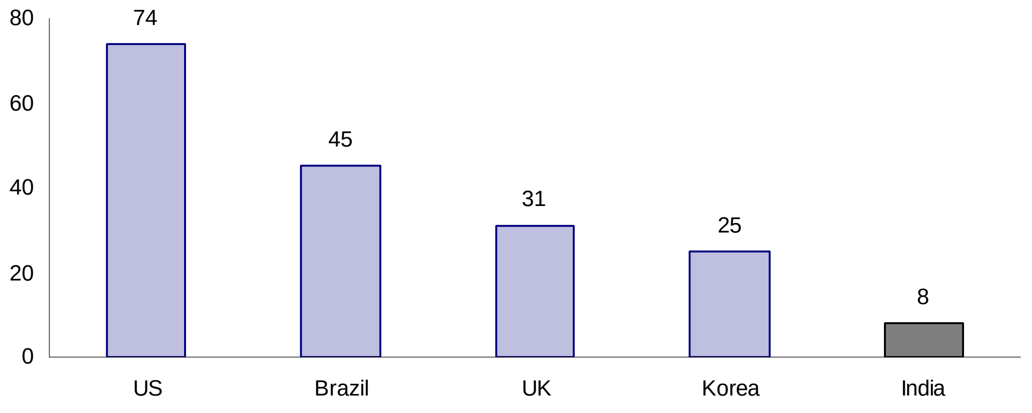
Asset management: largest player

Value/share of RCFT:	Rs259
Rs m	63,870
US$b	1.6
% of SOTP Value:	17

Reliance Asset Management Company (RAMC), a 100% subsidiary of RCFT, is the largest and fastest growing AMC in India. The AMC is present across products - mutual funds, portfolio management and offshore fund management services.

We believe the asset management business has tremendous growth opportunities on the back of robust GDP growth, rising income levels, increasing savings rate and lower penetration of fund management business in India. The Indian mutual fund industry is expected to grow its assets under management (AUM) at 35% in FY08 and FY09. We believe RAMC, with its proven track record of better than industry returns, stands to gain the most from this opportunity.

MF AUM PENETRATION (%)



Source: Company/Motilal Oswal Securities

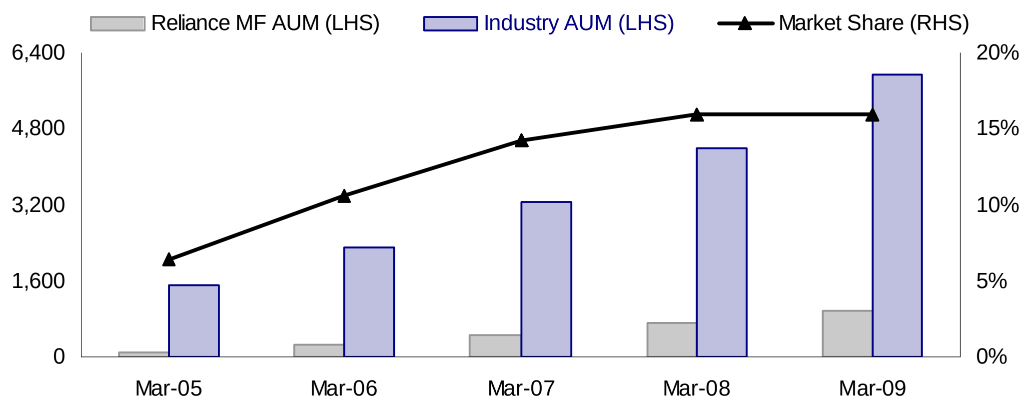
Already the largest mutual fund

Reliance Asset Management Company, RCFTs 100% subsidiary, is India's largest mutual fund in terms of assets under management

RMF is the number one mutual fund in India based on AUM. Its AUM surged to Rs599b (US$15b) in June 2007 from Rs477b (US$11) March 2007, mainly on account of aggressive mop-up of fixed maturity plans. Its market share in AUM has increased from 5% in March 2004 to 14% in March 2007 and 15% in June 2007.

GROWTH IN INDUSTRY AUM V/S RMF'S AUM (RS B)

We expect 16% market share for RMF, going forward



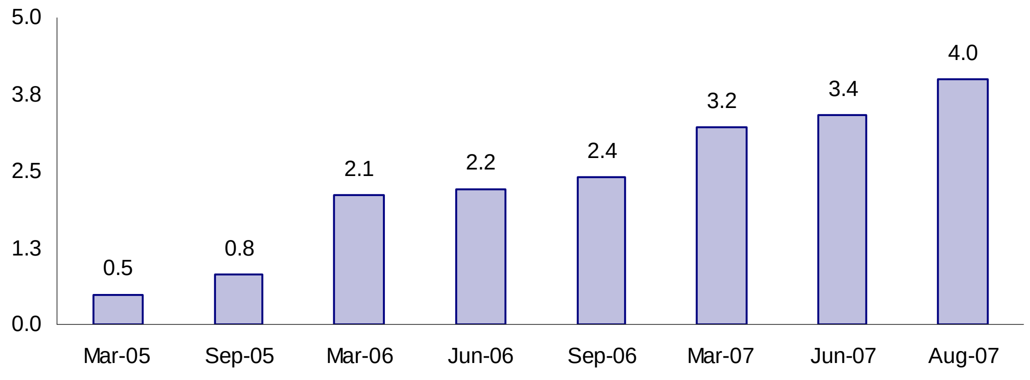
Source: Company/Motilal Oswal Securities

Largest customer base

It has 4m customers, the largest amongst private sector players

RMF enjoys the largest customer base amongst private mutual funds (4m as of August 2007), which has increased about eight times over in the last 28 months. We believe apart from the efficiency of the management team in generating returns, the success of any mutual fund also depends on the size of customer base. RMF already has more than 4m customers, which is the largest for any private mutual fund.

RMF: TREND IN NUMBER OF INVESTORS (M)



Source: Company/Motilal Oswal Securities

Leadership ingredients

We believe that the company will maintain its leadership in this business…

RMF aims to retain its leadership position in the industry by growing its AUM at least at the industry growth rate. It intends to be the most preferred investment choice for retail investors. We believe that (1) the performance and variety of schemes, (2) introduction of new ideas on a regular basis, and (3) customer reach and servicing are the three driving factors for growth in AUM and RMF has delivered on all the three parameters.

…given its robust performance…

1) Highly ranked performance track record: Reliance Growth Fund was ranked No.1 globally in terms of performance over a '5-year' and '10-year' period by Lipper in 2006. The fund also won the CNBC TV18-CRISIL Mutual Fund of the Year Award in the Open Ended Equity Diversified Fund category in 2006. Reliance Vision Fund was rated No.2 globally in the '5-year' category by Lipper in 2006. Its various income funds continue to be among the most consistent performers on the CRISIL~CPR list.

…diverse product offerings…

2) Product offering - diverse and growing: RMF offers 32 schemes (8 equity, 4 sector specific, and 20 debt/income). It launched eight new schemes in FY07 as against six new schemes in FY06. We believe the diverse basket of ideas and themes would enable the company to grow its AUM as well as number of investors by offering products that match different investment philosophies and mandates.

…and wide customer reach

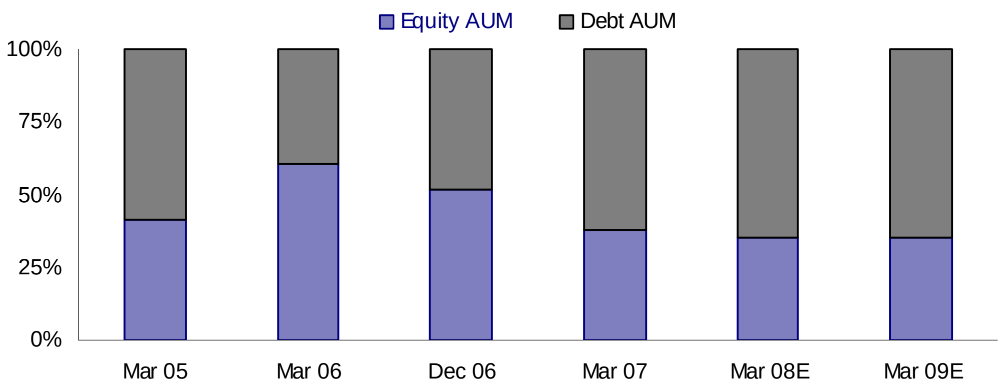
3) Customer reach and service: RMF has ~125 own branches (across 300 towns and cities) and we expect the branch network to expand rapidly. The strong customer base of 4m as of August 2007 confirms its deep retail reach. RMF has been adjudged as India's Most Trusted Mutual Fund Brand by Economic Times Brand Equity in a survey conducted by AC Nielsen ORG-Marg, in 2006. We believe RMF has the ingredients (capital , brand equity and performance track record) to further grow its customer base. It has launched innovative products like Reliance ATM card, which allows spot redemption, and facility to transact online through its website. We believe that the customer centric approach would facilitate its gaining customer patronage.

PMS and offshore fund: Though its Portfolio Management Service (PMS) was launched in August 2004, the company started focusing on growing its PMS AUM as another source of revenue only from FY06. Its AUM stands at Rs36b as of June 2007; about 2/3rd of its AUM is discretionary, which has a 'carry' element. We have factored in 5% above hurdle rate performance for FY08 and FY09 with a carry at 15%. We expect the PMS AUM to grow 100% in FY08 and 50% in FY09. The company has launched an India-dedicated US$125m equity growth fund as its first offshore fund in FY07. The fund carries 2% AMC structure with a carry of 15%. We expect the company to launch larger offshore funds in future. We have factored in a 100% AUM growth for offshore funds in FY08 and 50% in FY09.

Revenue and profitability

We expect RMF's AUM to grow 52% in FY08 and 35% in FY09. The equity AMC carries a higher fee (realizing 85-90bp on net basis) than the debt AMC (realizing 10-15bp on net basis).

RMF: AUM COMPOSITION



Source: Company/Motilal Oswal Securities

RAMC's revenue increased 118% in FY07 and we expect it to grow 79% and 51% in FY08 and FY09, respectively. We expect the equity AUM proportion to settle at ~35% in FY09. The 'carry' portion of PMS can provide further boost to our earnings estimate.

RMAC: REVENUE AND PROFITABILITY

	FY05	FY06	FY07	FY08E	FY09E
Total Income	503	935	2,037	3,654	5,499
YoY Growth (%)		*85.9*	*117.9*	*79.4*	*50.5*
EBITDA	190	451	741	1,705	2,806
EBITDA (%)	*37.8*	*48.2*	*36.4*	*46.6*	*51.0*
PAT	126	292	479	1,110	1,836
YoY Growth (%)		*131.5*	*64.0*	*131.8*	*65.3*

Source: Company/Motilal Oswal Securities

Valuation

We value RAMC based on its FY09 expected AUM. We value its equity AUM at 8%, debt AUM at 4%, and its PMS and offshore funds at 12% AUM. We arrive at a valuation of Rs63.9b for the business, implying a per share value of Rs259 for RCFT. This value represents 6% of total expected AUM of RAMC in FY09 and is 35x FY09E PAT.

RECENT AMC STAKE SALES

DATE	TARGET	ACQUIRER	STAKE (%)	AUM (RS B)	BUSINESS VALUED AT (RS B)	% OF AUM
Oct-05	Sundaram MF	BNP Paribas	50	28	2.0	7.2
Jan-07	Standard Chartered MF	UBS	100	136	5.3	3.9
Mar-07	CanBank MF	Robeco	49	22	2.4	10.9

Source: Company/Motilal Oswal Securities

- We believe that the valuations for Standard Chartered Mutual Fund were low as it had a higher proportion of debt AUM (close to 80%) and thus was a less profitable. Also, the StanChart management wanted to exit the business.
- CanBank MF, despite having predominantly debt schemes and a very small corpus, could fetch an attractive price because it had 'customer reach' through the 2,200+ branch network of Canara Bank.
- We believe the Sundaram-BNP deal provides a fair precedent transaction.
- We believe Reliance Mutual Fund could fetch significant premiums due to its brand, size and customer reach, if it were to dilute its stake.

Life insurance: fast gaining market share

Value/share of RCFT:	Rs624
Rs m	153,705
US$b	3.8
% of SOTP Value:	40

Reliance Life Insurance (RLI) had acquired AMP Sanmar for Rs1b in October 2005 to foray into the rapidly growing life insurance business. RLI introduced its first product in July 2006 and was one of late entrants into the business. At the time of the takeover, it had 90 offices, 9,000 agents and over 900 employees.

RCFT owns 16% direct stake in Reliance Life but 100% economic interest

RCFT has 100% economic interest in Reliance Life Insurance

RCFT has invested in the life insurance venture through two associate concerns (Viscount Management Services Ltd and Viscount Management Services (Alpha) Ltd, in each of which RCFT has a 50% stake), while keeping its own direct stake limited to 16%. The company has subscribed to zero coupon convertible unsecured debentures of these associates. The proceeds of these debentures have been invested in the equity of RLI. Thus, technically the company has avoided consolidation of RLI that is bound to make accounting losses in its initial growth phase.

Rapid 'reach' expansion

Currently the sixth-largest amongst private sector life insurance companies…

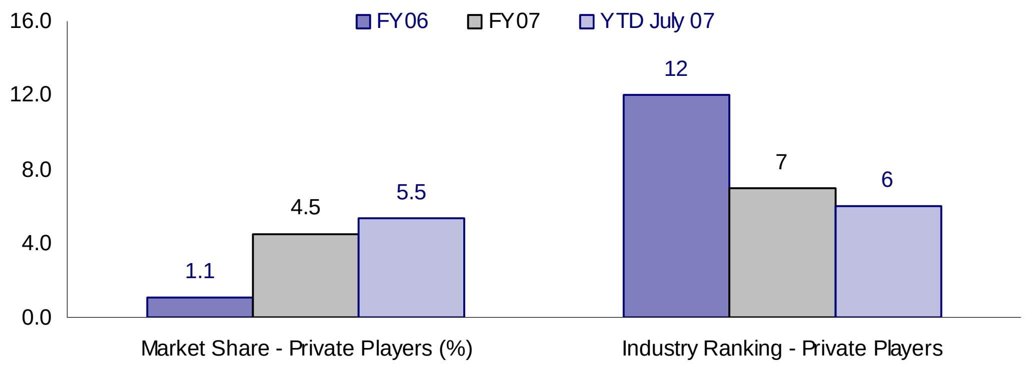
RLI has revitalized its business over the last year by adding manpower (over 7,000 employees as of date) and fast expansion of branch and agent network (342 branches and 127,317 agents as of June 2007). The company sees the agent force as the key driver for its revenue growth. Additional capital of Rs4b has been infused since takeover through various RCFT group companies. RLI aims to be among the top three private life insurance players by 2010. Reliance Life is currently the sixth largest private player in India based on APE YTD July 2007.

Strong business growth

…it intends to be one of the top-3 players in the business

The expansion and brand positioning efforts have paid off well, as evident from the sharp increase in the market share of the company.

RLI: GAINING MARKET SHARE (APE BASED)

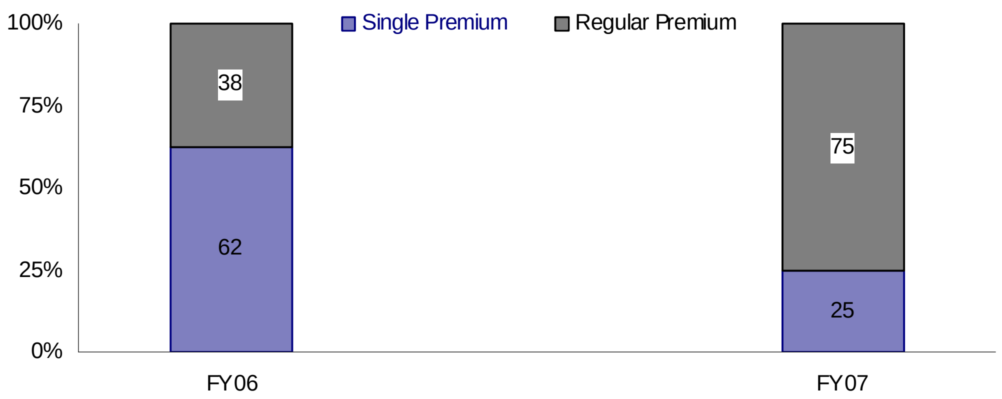


Source: Company/Motilal Oswal Securities

The total first year premium has jumped from Rs1.9b in FY06 to Rs9.3b in FY07. The company aims to triple this figure to Rs30b in FY08. The premium composition has moved in favor of Regular Premium Policies that are relatively more profitable and ensure revenue stability in future years.

Regular premium products now constitute 75% of its premium income

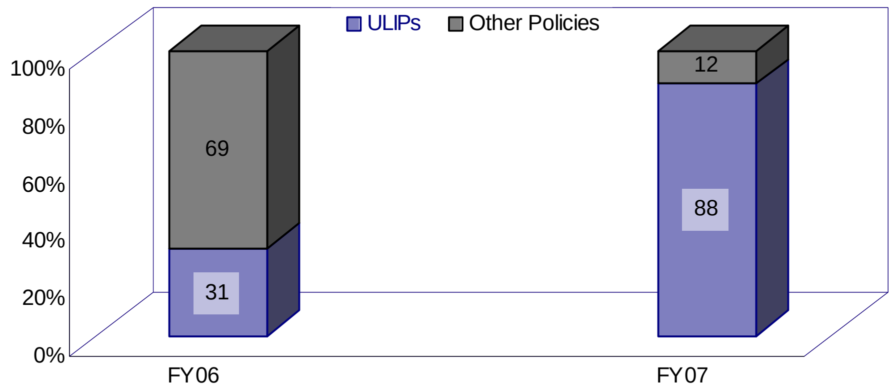
RLI: TREND IN PREMIUM COMPOSITION



Source: Company/Motilal Oswal Securities

The growth in premiums for RLI is mainly driven by ULIPs, which is in line with the industry.

RLI: ULIPS DRIVE GROWTH

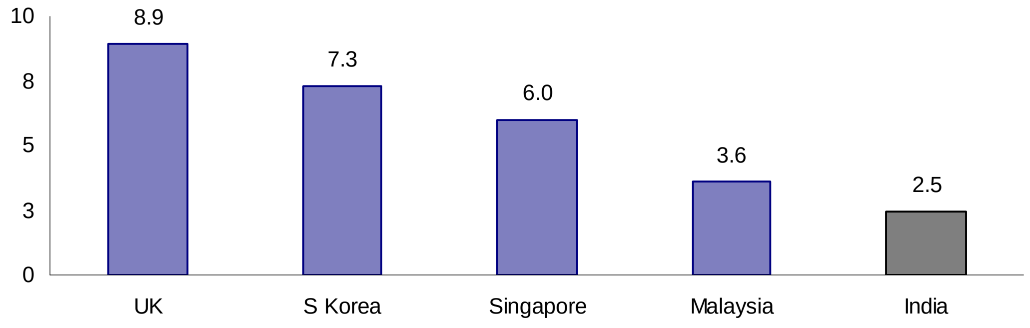


Source: Company/Motilal Oswal Securities

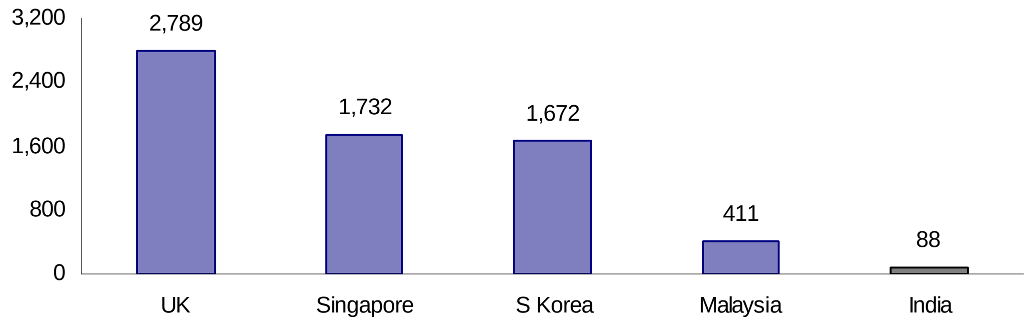
Strong sector outlook - Reliance Life gaining market share

- Currently, India has one of the lowest insurance penetrations in the world at ~2.5%. However, as the macro economic picture is benign, we expect the insurance industry to experience super normal growth over the next couple of years, resulting into penetration of 6-7% by FY09/FY10.

INSURANCE PREMIUM AS A % OF GDP



PER CAPITA INSURANCE PREMIUM (US$)



Source: Company/Motilal Oswal Securities

- RLI management has committed to emerge among the top-3 players in this industry by 2010. Given the execution track record of the Reliance ADAG (in communication and asset management business), we expect the management to further augment market share. Our belief is strengthened by the following: (1) The exceptional growth (in manpower, branch network and agent force as well as premium income and market share) achieved in just one and half years of full-fledged operations, (2) the massive agents and branch expansion plans, (3) capital infusion plans of Rs12-13b over the next 2-3 years, and (4) recently launched aggressive marketing campaign.
- The current 45m customer base of Reliance ADAG through its various businesses offers a ready pool of prospective policy holders for RLI.
- RCFT has sufficient financial muscle to provide any capital assistance to RLI in its initial growth phases (when it is expected to post higher accounting losses).

Valuation

We expect the APE to grow at a CAGR of 143% over FY07-09E

We expect the APE to grow at a CAGR of 143% over FY07-09E. We expect the growth to slow down progressively for succeeding years. We assume a lower NBAP margin of 17-18% (v/s 19% for Pru ICICI) considering its high cost of customer acquisition and spend on network expansion being a late entrant in this business. We value this business at 20x FY09E NBAP and arrive at Rs154b for the insurance venture. This implies a per share value of Rs624 for RCFT.

General insurance: fastest growing player

Value/share of RCFT:	Rs126
Rs m	31,060
US$b	0.8
% of SOTP Value:	8

Reliance General Insurance (RGI) mainly catered to Reliance group till FY06. Therefore, its revenue remained stagnant. Most of the fire (20% retention in FY06), marine (~40% retention in FY06) and engineering insurance (~20% retention in FY06) was ceded to other insurance companies, for which RGI earned heavy commissions. Lower provisions for unexpired risk reserve (on account of lower/no growth in revenue) and net commission earned (instead of commission expense) due to higher ceding in fire, marine and engineering business (comprising 51% of gross written premium (GWP) in FY06) helped the company to post profits.

What has changed?

RCFT's general insurance venture has now begun focusing on retail customers

The company realigned its focus to concentrate on retail products like motor and health insurance from FY07. It aims to be among the top-2 private players in general insurance domain in 2-3 years. The focus area would be retail customers.

Fast expanding distribution channels

The company has undergone fast branch expansion and employee additions to achieve its target position in FY08. The branch network increased to 85 in 44 locations as of March 2007 (ICICI Lombard had 220 branches as of March 2007). The number of intermediaries selling RGI products has increased from 787 in March 2006 to 18,300 in March 2007 and 36,463 in June 2007. The employee base of the company has increased to about 1,750 in June 2007 (ICICI Lombard had an employee base of 4,770 while Bajaj Allianz had an employee base of 2,540 as of March 2007).

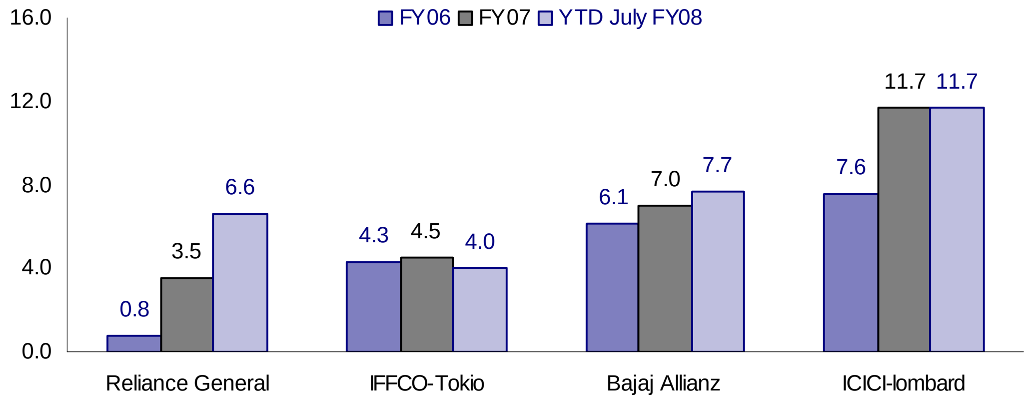
Banc assurance models have been highly successful for ICICI Lombard as well as Bajaj Allianz. The former has tie-ups with ICICI Bank, ABN Amro, American Express and Centurion Bank while the latter has tie-ups with UTI Bank, IDBI Bank, United Bank of India, Yes Bank, and Deutsche Bank. RGI being a late entrant would tend to lose on this mode of distribution initially. However, we believe the large number of franchisees planned for Reliance Money would partly compensate for the same.

Results already visible

Its market share has risen from just 0.8% in FY06 to 3.5% in FY07

Within just 12 months of renewed focus on this business, RGI has been able to achieve a market share of 3.5% in FY07 from 0.8% in FY06. It has emerged as the third largest private player in the industry on GWP basis, behind ICICI Lombard and Bajaj Allianz in YTD July 2007.

RGI: GAINING MARKET SHARE (%)

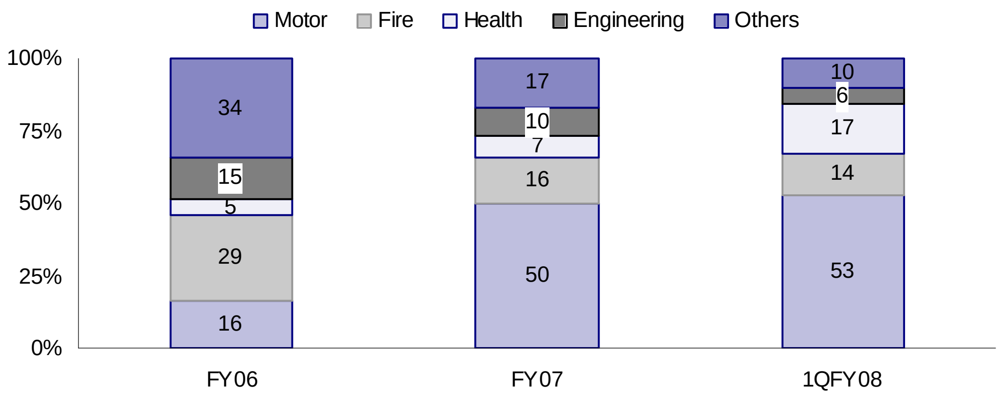


Source: Company/Motilal Oswal Securities

The GWP of the general insurance industry increased by 23% and that of private players increased by 60% in FY07, while RGI's GWP surged 461%. Thus, the company is the fastest growing general insurance company in India, though on a very small base. The company aims to grow over 100% in GWP in FY08 and be among the top-2 private players in the industry in 2-3 years - it has emerged as the third largest private player in YTD July 2007.

The focus to move portfolio to retail products has started showing results, as the share of health and motor insurance in GWP has increased to 57% in FY07 from 21% in FY06.

RGI: GROWING RETAIL PORTFOLIO



Source: Company/Motilal Oswal Securities

The company aims to retain 80% (against regulatory permissible 85%) of the retail insurance on its books and cede the balance. Inversely, it targets to retain lower portions of the big contracts.

Revenue and profitability

Due to the accounting conventions of making provisions for unexpired risks and expensing costs upfront, we expect the company to report marginal profits in FY08 since it is in the hyper growth phase. Though the company currently has a combined ratio of 94% (lower than ICICI's 97% and Bajaj's 98%), we expect the ratio to come in line with the industry over the next two years. Thus, we assume 97% combined ratio for FY09, implying Rs3 underwriting profit on every Rs100 of net premium written. We believe the economic profit measure captures the profitability of the company better than the accounting profit.

Valuation

We value this business at 20x FY09E economic profit. This implies Rs31b of business value, which implies a Rs126 per share value for RCFT.

Broking & distribution: a great business

Value/share of RCFT:	Rs95
✍ Rs m	23,478
✍ US$b	0.6
% of SOTP Value:	6

RCFT has entered the broking and distribution business through its sister concerns under the brand name Reliance Money (RM). RM was formally launched in April 2007 with 2,270 outlets in over 625 locations. The value propositions that RM is offering to its customers are 'all products under one roof', 'variety of access channels', and 'lower charges by way of flat fees' for broking. The business model is to increase 'revenue per customer' by selling to a customer a host of financial products once he becomes a 'RM customer' in any segment. Though brokerage income would be limited considering the penetrative pricing adopted by the management, distribution income would be a key revenue driver.

The investment in this business is held indirectly through group companies to avoid consolidation of its operating results till the business attains material scale and profitability.

Offering entire gamut of services ...

Reliance Money intends to own the retail customer and offer him all financial services under one roof

The products and services offered by RM are:

- equity, equity and commodity derivatives, D-mat services
- distribution of mutual funds (all MFs and not limited to RMF alone), IPOs, life and general insurance (products from all insurance companies)
- offshore investments and advisory, wealth management
- money transfer and money changing (through Travel Mate)
- credit cards and financing (through parent Reliance Capital)

RM's model is to 'own the retail customer and offer him all the services under one roof'. Initially, the focus is to get a large number of customers on board through penetration pricing and grow the revenue per customer thereafter.

... through multiple channels

As at June 2007, it had set up 4,000 outlets covering 700 towns and cities

The company is focusing on the franchisee model for network expansion. It started by setting up 2,270 outlets covering 625 towns and cities in April 2007. In June 2007, the network stood increased to 4,000 outlets in 700 locations. Additionally, 2,500 kiosks have been installed as an alternative channel for accessing customers. RM is targeting tier-II and tier-III cities as well as they remain under-penetrated so far. Though the company has started by adopting a franchisee model (to keep costs lower), the management is aiming to set up its own branches in due course of time. Management guides of setting-up 1,000 own branches by FY09.

Points of contact (apart from franchisees):

- Online trading
- Kiosks, which connect to RM website, would be set up at high footfall locations like malls and multiplexes
- It has already set up a 350-seater dedicated call center to offer 'call and trade' facility and address customer complaints

Focus on customer acquisition and volume

The company aspires to be among India's top-2 brokerage houses in terms of volume by FY10

We believe RM can leverage on the strong customer base of Reliance Communication (35m customers), Reliance Energy (5m customers) and Reliance MF (investor base of 4m). Customer acquisition and increasing market share are the key focus areas of the management in the initial few years of launch. RM has 150,000 customers currently and is clocking an average daily turnover of Rs6b in trading volume. It is adding ~1,000 customers per day. The company aspires to grow by volume and emerge among the top two brokerage houses by volume in India by FY10.

Broking charges abysmally low; revenue per customer to be increased

While its broking charges are abysmally low…

RM is looking to acquire clients by offering ~90% lower than industry average broking rates (brokerage rate of 0.05% against industry average of 0.5% for delivery based contracts and brokerage rate of 0.005% against industry average of 0.05-0.1% for non-delivery based contracts). It has launched a prepaid card of Rs500 valid for two months, which allows the customer to trade up to Rs1m in delivery based contracts or Rs10m in non-delivery based contracts. As the non-delivery (intra-day) segment of the market is sensitive to brokerage rates, we believe there would be faster accretion of customers from this segment.

…the company hopes to increase revenue per customer through cross-selling of products

However, the company sees more opportunity in cross selling of financial products and services to increase revenue from a customer. It focuses on owning the customer for all his financial needs. RM has guided for Rs350-400 per month average revenue per customer in FY09.

Key success facilitators in place

We expect Reliance Money's low-fee, high-volume business model to succeed

- Macro economic conditions and indicators augur well for growth considering lower penetration of financial products like insurance, equity and related assets among households. Rising disposable income, increasing savings rate and growing awareness of financial products would ensure financial distribution and broking businesses see high growth in the years to come.
- Management has a proven track record of execution in 'growing by volume' business model.

- The current customer base of 35m from Reliance Communication, 5m from Reliance Energy and 4m investors of RMF offer a ready pool of prospective customers.
- We believe the broking industry would be dominated by large players and smaller players would get marginalized or get aligned with the larger ones. Already 25% market share within retail is with the top ten brokers.
- The penetration pricing policy (90% lower pricing, purely on brokerage rate comparison) would help the company in acquiring customers fast.

However, we expect the revenue and profit to be lower in the first two years of operations. This is because the revenue per customer would remain lower on account of the penetrative pricing policy and spend on advertisement and establishment. Eventually, as the company is able to increase the brand loyalty by being able to satisfy every financial need of its customers (except banking), the average revenue per customer would tend to increase.

Revenue and profitability

We estimate a PAT of Rs945m for FY09 and Rs1,800m for FY10

Management is targeting 400,000 customer base by FY08 and 1m customer base by FY09 with revenue per customer of Rs350-400 in FY09 per month. We have factored in a customer base of ~0.7m in FY09 and average revenue of Rs375 per month per customer. We have assumed a net profit margin of 25% in FY08 and 30% in FY09 and FY10 considering the franchisee based and technology-driven model adopted by the company. We expect a PAT of Rs945m and Rs1,800m in FY09 and FY10, respectively.

BROKING AND DISTRIBUTION

REVENUE STATEMENT	FY08E	FY09E	FY10E
Customer Base target (in thousands)	350	700	1,000
Average Revenue Per Customer (Rs pm)	300	375	500
Revenue (Rs m)	1,260	3,150	6,000
PAT margin (%)	25.0	30.0	30.0
PAT (Rs m)	315	945	1,800

Source: Company/Motilal Oswal Securities

Valuation

We value this business at 15x FY10E earnings and discount the value to FY09 at 15% rate, as we believe RM is still in the start-up phase and meaningful profits are likely to accrue only from FY10. However, post FY10, as the incremental investment in business reduces; we expect strong growth in profitability. Our valuation for RM is Rs23b, implying Rs95 per share of RCFT.

Financing business: next big earnings driver

Value/share of RCFT:	Rs242
Rs m	59,621
US$b	1.5
% of SOTP Value:	15

RCFT completed the circle of retail financial services by launching its consumer finance business in the four metros during 1QFY08. RCFT has a strong net worth of Rs55b and unrealized gains on listed investments of Rs35b. RLI, RGI and other businesses together would require additional investments of Rs15-16b over the next 2-3 years. The surplus net worth of Rs29-30b would enable company to aggressively borrow in bulk market and lend to retail customers. The company wishes to focus on four key areas of financing viz. mortgages, vehicle loans, personal loans and SME. However, it does not intend to get involved in sub-prime lending.

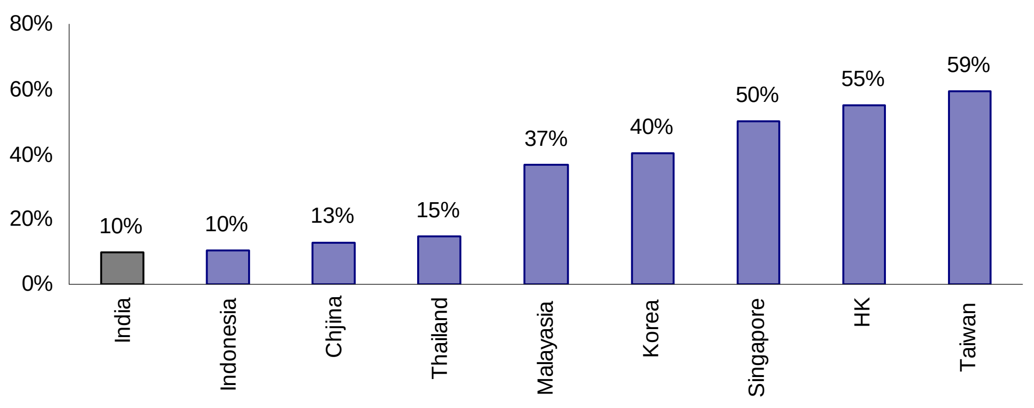
RCFT can take 6-8x leverage on its equity and build its loan portfolio. The company would typically earn 15%-16% average yield on its loan portfolio while we believe its average cost of borrowing would be 12%-13%. We assume the company will begin the financing business with an initial commitment of Rs11b and increase it to Rs18b in next two years.

Macro outlook positive

Retail credit is an under-penetrated market in India…

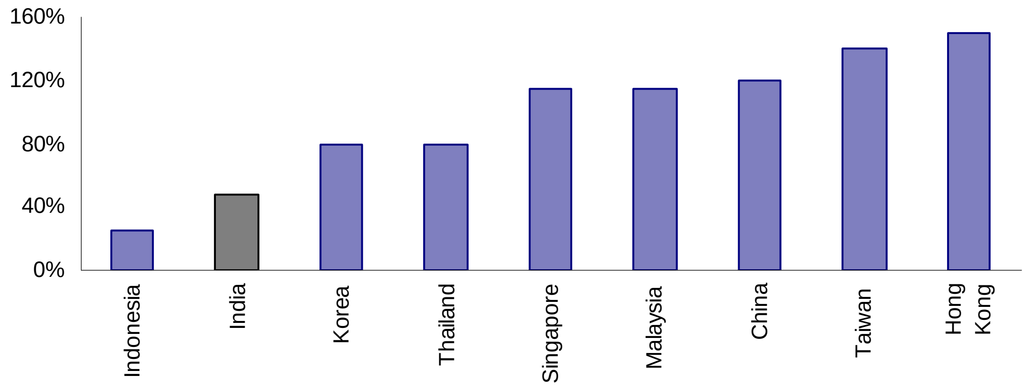
Despite its fast pace of growth, retail credit is under-penetrated in India. We believe it would continue to grow at a fast pace going forward, though some short-term slow-down may be observed. In the current regulatory scenario, an NBFC like RCFT is better placed to undertake retail financing in a profitable manner, as it is absolved from SLR and CRR requirements. Further, the aversion of state-owned banks to retail financing offers an opportunity for RCFT to aggressively build this business. The robust corporate credit demand outlook on the back of huge investments expected in infrastructure and manufacturing sector makes SME finance an equally attractive proposition.

CONSUMER LOAN TO GDP RATIO



Source: Company/Motilal Oswal Securities

LOANS/ GDP RATIO (%)



Source: Company/Motilal Oswal Securities

Revenue and profitability

…and offers a huge opportunity for RCFT

RCFT is likely to commit Rs11b equity to this business in FY08 and would take a leverage of 3x in FY08 and gradually increase it to 6x-7x in succeeding years. We assume another Rs7b equity infusion in this business over next 2 years.The normalized NIMs would be ~5.5% for the business. We assume ~2% of the loan book being written off as bad loans for each of the years. The company guides of loan book of Rs200b by FY09E and Rs400b by FY10E with a RoA of 1.5% by FY09E. However, we are building a loan book of Rs100b and an RoA of 1.1% in FY09E.

FINANCING BUSINESS: REVENUE STATEMENT (RS M)

	FY08E	FY09E	FY10E	FY11E
Interest Income	5,040	11,360	26,400	41,019
Interest Expense	3,101	7,028	17,364	27,907
Net Interest Income (NII)	**1,939**	**4,332**	**9,036**	**13,112**
Operating Expenses	882	1,103	1,378	1,723
Bad Loans	630	2,000	4,400	5,544
PBT	427	1,229	3,258	5,845
Tax	141	406	1,075	1,929
PAT	286	823	2,183	3,916
RoA (%)	0.6	1.1	1.3	1.5
RoE (%)	2.6	4.7	7.8	11.5
NIM (%)	4.6	6.1	5.6	5.3
NIM post bad loans (%)	3.1	3.3	2.9	3.0

Source: Company/Motilal Oswal Securities

BALANCE SHEET ABSTRACT (RS M)

	FY08E	FY09E	FY10E	FY11E
Liabilities				
Net Worth	11,025	23,848	32,031	35,947
Funds Borrowed	33,075	79,380	198,450	248,063
Debt to Equity	3	3	6	7
Total	**44,100**	**103,228**	**230,481**	**284,010**
Loans Given	42,000	100,000	220,000	277,200
Cash and Equivalents	2,100	3,228	10,481	6,810
Total	**44,100**	**103,228**	**230,481**	**284,010**

Source: Motilal Oswal Securities

Valuation

Over the next three years, we expect the RoA to settle around 1.5%, NIM around 5.5%. We value this business at 2.5x its FY09E BV. We arrive at a valuation of Rs60b for the consumer finance business, representing Rs242 per share of RCFT.

New ventures on the anvil

Asset reconstruction company: early mover advantage

RCFT has floated an Asset Reconstruction Company (49% stake for Rs0.5b) in partnership with GIC, Corporation Bank and Indian Bank. However, it has yet to receive approval from RBI to commence operations. Rajendra Kakkar; ex-CEO of ARCIL, would be heading the company. We believe RCFT will have an early mover advantage in this business. However, we feel it is too early to value this business.

Banking; investment banking: on the drawing board

Banking: Post 2009, whenever RBI allows corporate groups to enter the banking business, Reliance Capital is likely to apply for a licence. It could either float a banking subsidiary or acquire some bank. We believe that the banking business would complete the whole gamut of financial services which Reliance Capital could offer. Also, given its distribution network in asset management, life insurance and Reliance Money by FY09, we believe that the banking business has potential to create huge scale in a short period of time.

Investment banking: The management has highlighted its plans to start investment banking. It has applied for its investment banking licence. However, as of now Reliance Capital has not yet put a team in place, though the management is keen to start this business over the next 6-18 months.

Investment book and surplus networth: hidden value

RCFT has strategic investments in Reliance group companies and Adlabs. The company plans to dispose off these investments as and when its own businesses require capital. Based on investment status as of March 2007 and current market price, the unrealized gains on these investments are Rs35b, implying Rs143 per share of RCFT. The shares in Adlabs with current value of Rs9.7b are held in the name of an associate (Reliance Land Ltd). RCFT funded this acquisition by giving a loan to Reliance Land.

UNREALIZED GAINS ON INVESTMENTS (RS M)

INVESTMENT BOOK	NO OF SHARES	COST	UNREALIZED GAINS
Adlabs Films (Consolidated Holding)	21,855,000	3,705	6,589
Reliance Inds.	9,355,295	1,147	17,185
Reliance Comm	18,440,295	2,091	7,923
Reliance Natural	16,471,295	27	721
Entertainment Network	123,000	38	20
Global Broadcast News	1,800,000	845	632
IDFC	10,000,000	720	532
Others		3,559	1,584
Total		**12,130**	**35,187**

CALCULATION OF FREE NET WORTH	(RSM)	REMARKS
Networth (FY07, fully diluted)	**53,024**	
Less: Investments in Businesses		
Life Insurance	16,000	Current capital of Rs5b, likely to rise to Rs16b by FY09
General Insurance	3,000	Current capital of Rs1b, likely to rise to Rs3b by FY09
Broking and distribution	1,000	Broking would require Rs1b of capital
Consumer Finance	18,000	In order to build the consumer finance book, assumed equity infusion of Rs18b by FY09E
Stake in Adlabs through Reliance Land	3,580	Actual Investment held in Reliance Land
ARC and others	1,200	
Total Networth required for other bus.	**42,780**	
Surplus Networth as of FY07	10,244	
Valuing at 2x	20,488	
Per share value (Rs/Sh)	83	

Source: Motilal Oswal Securities

We believe that its investment book and free net worth will not only help the company to smoothen its earnings over the next couple of years but would also be sufficient to fund the incremental equity capital needs of Reliance Life (Rs11b) and Reliance General (Rs2b). Thus, in our view, any dilution in equity over the next three years is ruled out for organic growth.

PROFIT AND LOSS ACCOUNT (CONSOLIDATED)				(RS MILLION)
	FY06	FY07	FY08E	FY09E
Revenue				
Finance and Investments	6,520	8,983	11,193	13,054
Asset Management	935	2,038	3,654	5,499
General Insurance GWP	2,027	10,559	18,195	29,357
Finance Business (NII)	0	0	1,939	4,332
Total Revenue	**9,482**	**21,579**	**34,981**	**52,241**
EBITDA				
Finance and Investments	6,190	7,829	9,925	11,460
Asset Management	451	741	1,705	2,806
General Insurance Operating Profit	110	-135	12	1,348
Financing Business	0	0	1,057	3,229
EBITDA	**6,751**	**8,435**	**12,699**	**18,843**
PBT				
Finance and Investments	5,506	7,374	8,855	10,310
Asset Management	438	719	1,682	2,781
General Insurance	211	22	176	1,530
Financing Business	0	0	427	1,229
PBT	**6,155**	**8,115**	**11,141**	**15,851**
PAT				
Finance and Investments	5,376	6,462	7,615	8,867
Asset Management	292	479	1,110	1,836
General Insurance	144	16	118	1,025
Financing Business	0	0	286	823
Misc Adjustements	6	41	0	0
Total PAT	**5,819**	**6,997**	**9,130**	**12,551**
% Growth		*20.3*	*30.5*	*37.5*
Minority Interest	35.9	0	-	-
Share of Profits from Associates	-68.9	34.9	-	-
PAT for Shareholders	**5,714**	**7,032**	**9,130**	**12,551**
Dividend	713	860	963	1,231
Tax on Dividend	100	146	144	185
Net Retained Profit	**4,901**	**6,026**	**8,022**	**11,136**

E: MOSt Estimates

BALANCE SHEET (CONSOLIDATED)				(RS MILLION)
	FY06	FY07	FY08E	FY09E
Liabilities				
Net Worth	**42,114**	**53,024**	**61,170**	**72,182**
Equity	2,234	2,462	2,462	2,462
Warrants	495	0	0	0
Reserves and Surplus	39,385	50,562	58,584	69,720
Minority Interest	387	0	0	0
Loan Funds	2,419	14,030	48,075	101,380
Secured Funds	1,675	1,450		
Unsecured Funds	744	12,580		
Deferred Tax Liability	9	75	75	75
Total Liabilities	**44,929**	**67,129**	**109,196**	**173,6377**
Assets				
Fixed Assets	**1,902**	**1,390**	**1,515**	**1,797**
Gross Block at the Beginning of the Year	5,521	3,906	3,480	3,980
Additions / Deductions During the Year	-1,614	-426	500	500
Depreciation to Date	2,136	2,291	2,465	2,683
Capital Work in Progress	131	199	0	0
Net Block at the End of the Year	1,902	1,390	1,515	1,797
Investments	23,938	28,531	31,384	37,660
Loans and Advances	0	0	42,000	100,000
Current Assets	**21,282**	**44,327**	**45,644**	**47,728**
Cash and Bank	2,016	2,121	2,730	3,809
Sundry Debtors	777	2,776	3,332	3,998
Loand and Advances	12,239	37,583	37,583	37,583
Stock for Trade	62	307	307	307
Other Current Assets	6,189	1,539	1,693	2,032
Less: Current Liability	**2,255**	**7,169**	**11,387**	**13,581**
Current Liabilities	1,024	3,065	4,000	2,500
Provisions	1,232	4,104	7,387	11,081
Miscelleneous Expenditure	62	50	40	32
Total Assets	**44,929**	**67,129**	**109,196**	**173,637**
Valuation Ratios				
Book Value (Rs)	188.5	215.4	248.0	293.2
EPS (Rs)	25.6	28.6	37.1	51.0
P/E (x)	46.9	42.0	32.3	23.5
P/BV (x)	6.4	5.6	4.8	4.1
RoA (%)	-	12.6	10.4	8.9
RoE (%)	-	14.8	16.0	18.8

E: MOSt Estimates

N O T E S

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Disclosure of Interest Statement	Reliance Capital
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No