

## RELIANCE CAPITAL

INR 1,809

*We recommend a breather*

REDUCE

Reliance Capital has witnessed three-fold rise in its stock price during the past six months, led by exponential growth in its existing businesses and strong traction in new businesses.

\* **What lies ahead?....very strong business growth**

We are positive on the company's overall business performance and expect its asset management segment to grow by 45% over FY07-10E, market share in life insurance to improve significantly to 10% by FY09E and 11% in FY10E, and the GWP in general insurance to grow aggressively at 100% plus over FY07-09E. Moreover, we estimate the company's retail broking business to generate a profit of INR 1,050 mn by FY09E and INR 1,575 mn by FY10E, and its consumer finance book to grow to INR 115 bn by FY09E and INR 185 bn by FY10E.

\* **Do current valuations capture medium-term visibility in its businesses? Yes**

We believe the stock's recent performance has priced-in aggressive growth targets in existing businesses and also captures the possibility of the company venturing into complementary businesses like investment banking, institutional broking, asset reconstruction, etc. Our sum-of-the-parts (SOTP) framework gives us the base case fair value of INR 1,573 on FY09E and INR 1,874 on FY10E estimates and we believe the stock should hover in this range in the medium term. *We, therefore, recommend investors to book profit at these levels and to view any weakness in the stock as an opportunity to re-enter.* We believe Reliance Capital's stock price has always included some "sure execution premium", which has increased significantly. *If we assign 100% probability to what the company seeks to achieve over the next two years, we arrive at the fair value of INR 1,894 on FY09E estimates and INR 2,482 on FY10E basis (best case).*

\* **What you are likely to miss if you book profits now?**

The company currently owns 100% of the life insurance, general insurance, and AMC businesses. These businesses have achieved significant scale and the company could now possibly resort to minority stake sale and get in new partner(s). Moreover, listing or strategic stake sale of its broking arm may be a possibility.

We have not built in the valuation of expected-to-be-launched businesses—investment banking, institutional broking, asset reconstruction, and re-insurance business. Again, visibility on the same is lacking at this moment.

## SOTP valuation

Businesses	Method	Value /share	Value /share
		FY09E (INR)	FY10E (INR)
Asset management / PMS / Offshore	% of AUMs	303	380
General Insurance	Economic profit multiple	150	225
Life Insurance	Appraisal value	633	728
Excess network	P/B	81	9
Unrealised gain on invest. in shares	Market value	187	187
Retail broking business	P/E	77	115
Consumer finance business	P/B	142	229
<b>Fair Value</b>		<b>1,573</b>	<b>1,874</b>



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Bloomberg : RCFT IN

## Market Data

52-week range (INR) : 1,889 / 530  
Share in issue (mn) : 245.6  
M cap (INR bn/USD mn) : 444 / 11,130  
Avg. Daily Vol. BSE/NSE ('000) : 2,247.3

## Share Holding Pattern (%)

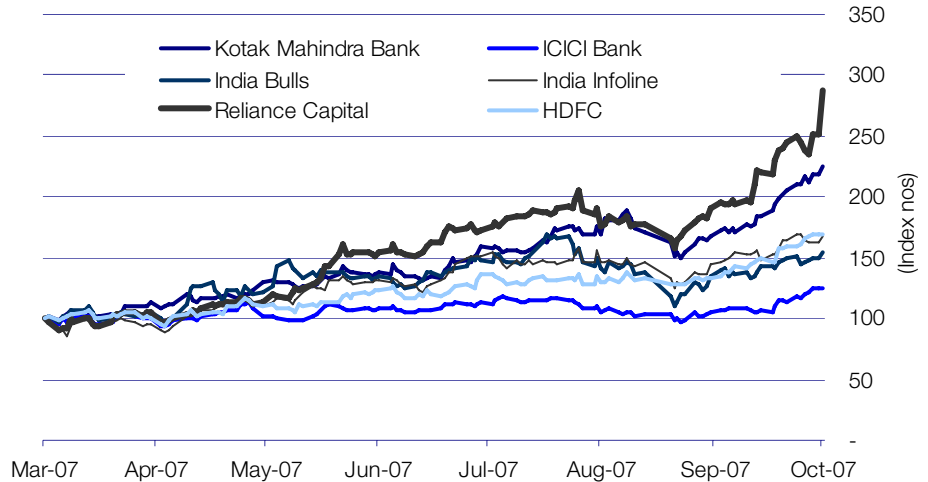
Promoters : 52.4  
MFs, Fls & Banks : 2.7  
FII : 29.9  
Others : 15.0



**\* Three-fold increase in stock price in a span of six months...**

Reliance Capital has outperformed almost all stocks in the financial services space during the past six months. The stock rose three-fold during this period (we initiated coverage in March 2007 at INR 640) and has outweighed our and Street's expectations over the past two quarters.

**Chart 1: Reliance Capital has outperformed its peers**



Source: Bloomberg

**Table 1: Relative stock performance**

(%)	Reliance Capital	Kotak	HDFC	Indiabulls	India Infoline	ICICI Bank
1 Month	50.8	33.8	26.9	14.9	27.6	19.6
3 Months	66.2	40.6	23.6	4.8	21.5	10.8
6 Months	171.7	97.4	67.1	48.0	159.7	25.4
1 Year	217.9	185.3	65.6	255.1	369.9	53.0

Source: Bloomberg

**\* ...led by exponential growth in its existing businesses and strong traction in new businesses**

We believe, key triggers of Reliance Capital's stupendous performance on the bourses were:

**◆ Exponential growth in existing businesses**

- ◆ 50% YTD growth in mutual fund AUM; it has crossed the INR 700 bn mark (compared with 33% YTD growth for Pru ICICI and 27% for UTI MF).
- ◆ Improved market share in life insurance to 5.8% (from 4.9% in FY07), recording APE of INR 3.7 bn YTD (compared to INR 7 bn for FY07).
- ◆ Writing 17.5% of YTD industrywide gross premium in the general insurance segment (10% in FY07) and registering 200% YTD growth in GWP to INR 8.1 bn (INR 9.1 bn of GWP for FY07).

- ◆ **Newly launched businesses gaining strong traction**

- ◆ Reliance Capital's retail broking business (since its launch in April 2007) has gained strong traction; it is registering average daily trading volume of INR 11 bn (equivalent to volumes of India Infoline and compares favorably with other established players). Its retail customer base is in excess of 150,000.
- ◆ The consumer finance business has been launched in four metros and the company plans to have a pan-India presence in the near term.

- ◆ **Another key trigger has been active investor interest**

Created through increased coverage on the stock by a number of brokerage houses in the past few months, supported by phenomenal returns the stock has generated in the past one year. Many investors now view Reliance Capital as a pure play on the rapidly expanding financial services space (ex-banking).

- ◆ **Boost from group company stock price rally**

75-80% of the current value of Reliance Capital's quoted investments flows from Reliance Group companies, viz., Reliance Industries, Reliance Communication, Reliance Natural Resources, and Reliance Industries Infrastructure; the stock prices of which have seen a sharp rally, thereby boosting Reliance Capital's valuations.

- \* **What lies ahead? ...very strong business growth**

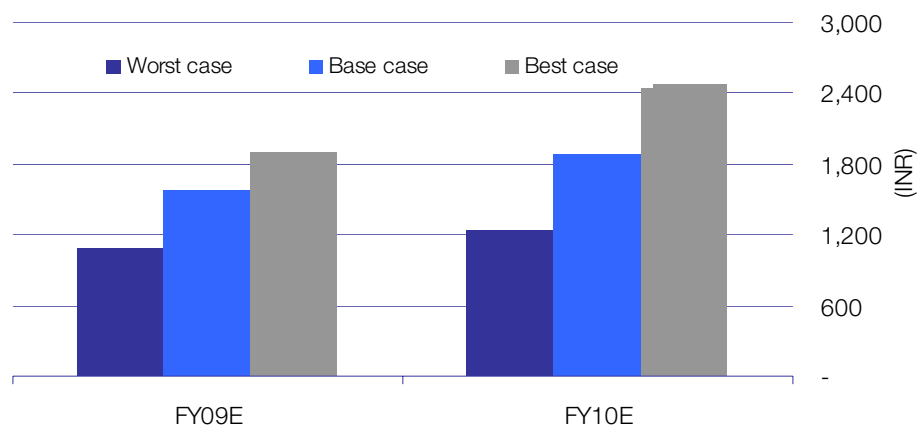
Undoubtedly, we are positive on the company's overall business performance. We expect its asset management segment to grow by 45% over FY07-10E, market share in life insurance to improve significantly to 10% by FY09E and 11% in FY10E, and the GWP in general insurance to grow aggressively at 100% plus over FY07-09E. Moreover, we expect the company's retail broking business to generate a profit of INR 1,050 mn by FY09E and INR 1,575 mn by FY10E, and its consumer finance book to grow to INR 115 bn by FY09E and INR 185 bn by FY10E.

- \* **Do current valuations capture medium-term visibility in its businesses? Yes**

Despite being positive on its business growth, the concern that current valuations defy near-term growth targets dominates our thought process at the price of INR 1,850 plus. We believe the stock's recent performance has priced-in aggressive growth targets in existing businesses and its endeavor to be the leader in the financial services space. The price also captures the possibility of the company venturing into complementary businesses like investment banking, institutional broking, asset reconstruction, etc. Our sum-of-the-parts (SOTP) framework gives us the base case fair value of INR 1,573 on FY09E and INR 1,874 on FY10E estimates and we believe the stock should hover in this range in the medium term. ***We, therefore, recommend investors to book profit at these levels and to view any weakness in the stock as an opportunity to re-enter.*** We believe Reliance Capital's stock price has always included some "sure execution premium", which has increased significantly.

***If we assign 100% probability to what the company seeks to achieve over the next two years, we arrive at the fair value of INR 1,894 on FY09E estimates and INR 2,482 on FY10E basis (best case).***

Chart 2: SOTP valuation in different scenario



Source: Edelweiss research

Table 2: SOTP valuation

## Base case scenario

Businesses	Method	FY09E				FY10E			
		Base value (INR mn)	Multiple	Value (INR mn)	Value per share (INR)	Base value (INR mn)	Multiple	Value (INR mn)	Value per share (INR)
Asset management	% of AUMs	1,124,768	6.0	67,486	274	1,405,960	6.0	84,358	343
PMS	% of AUMs	70,000	8.0	5,600	23	90,000	8.0	7,200	29
Offshore AUMs	% of AUMs	20,800	7.0	1,456	6	28,080	7.0	1,966	8
General insurance	PE	2,302	16.0	36,832	150	3,683	15.0	55,248	225
Life insurance	Appraisal value	6,074	25.6	155,650	633	8,391	21.3	178,945	728
Excess networth	PB	17,267	1.2	19,857	81	1,965	1.2	2,260	9
Unrealised gain on investment in shares	Market value			38,210	155			38,210	155
Unrealized gain on adlabs	Market value			7,927	32			7,927	32
Retail broking business	PE	1,050	18.0	18,900	77	1,575	18.0	28,350	115
Consumer finance business	PB	18,352	1.9	34,869	142	29,654	1.9	56,343	229
<b>Fair value</b>				<b>386,787</b>	<b>1,573</b>			<b>460,806</b>	<b>1,874</b>

## Best case scenario

Businesses	Method	FY09E				FY10E			
		Base value (INR mn)	Multiple	Value (INR mn)	Value per share (INR)	Base value (INR mn)	Multiple	Value (INR mn)	Value per share (INR)
Asset management	% of AUMs	1,300,000	7.5	97,500	397	1,755,000	7.5	131,625	535
PMS	% of AUMs	80,000	9.0	7,200	29	115,000	9.0	10,350	42
Offshore AUMs	% of AUMs	25,000	7.0	1,750	7	40,000	7.0	2,800	11
General insurance	PE	2,662	18.0	47,916	195	4,525	16.0	72,406	294
Life insurance	Appraisal value	7,020	25.0	175,500	714	11,250	21.0	236,250	961
Excess networth	PB	15,119	1.4	21,167	86	500	1.4	700	3
Unrealised gain on investment in shares	Market value			38,210	155			38,210	155
Unrealized gain on adlabs	Market value			7,927	32			7,927	32
Retail broking business	PE	1,700	18.0	30,600	124	2,550	18.0	45,900	187
Consumer finance business	PB	20,000	1.9	38,000	155	33,753	1.9	64,131	261
<b>Fair value</b>				<b>465,770</b>	<b>1,894</b>			<b>610,299</b>	<b>2,482</b>

## Worst Case Scenario

Businesses	Method	FY09E				FY10E			
		Base value (INR mn)	Multiple	Value (INR mn)	Value per share (INR)	Base value (INR mn)	Multiple	Value (INR mn)	Value per share (INR)
Asset management	% of AUMs	960,000	5.0	48,000	195	1,152,000	5.0	57,600	234
PMS	% of AUMs	60,000	8.0	4,800	20	75,000	8.0	6,000	24
Offshore AUMs	% of AUMs	8,400	6.0	504	2	12,600	6.0	756	3
General insurance	PE	1,400	16.0	22,400	91	1,890	15.0	28,350	115
Life insurance	Appraisal value	3,722	26.5	98,673	401	5,021	22.6	113,307	461
Excess networth	PB	22,119	1.0	22,119	90	11,119	1.0	11,119	45
Unrealised gain on investment in shares	Market value			30,568	124			30,568	124
Unrealized gain on adlabs	Market value			6,342	26			6,342	26
Retail broking business	PE	410	15.0	6,150	25	533	15.0	7,995	33
Consumer finance business	PB	15,000	1.9	28,500	116	22,000	1.9	41,800	170
<b>Fair value</b>				<b>268,056</b>	<b>1,090</b>			<b>303,837</b>	<b>1,236</b>

Source: Company, Edelweiss research

\* What you are likely to miss if you book profits now

- ◆ The company currently owns 100% of the life insurance, general insurance, and AMC business. These businesses have achieved significant scale and the company could now possibly resort to minority stake sale and get in new partner(s). This may act as a positive trigger and provide some benchmark valuation; but we believe this has been factored in the price. Moreover, listing or strategic stake sale of its broking arm may be a possibility.
- ◆ We have not built in the valuation of expected-to-be-launched businesses—investment banking, institutional broking, asset reconstruction, and re-insurance business. Again, visibility on the same is lacking at this moment.
- ◆ Venturing into complementary markets/businesses in financial services space has not been factored in at the current stage.
- ◆ Reliance Capital has huge exposure to the media/entertainment industry through investments in Adlabs Films, ENIL, Global Broadcasting, Inox Leisure, TV Today etc. These investments are warehoused in Reliance Capital for ADAG group and any integration/consolidation of or other similar developments in these investments (at the company level) could act as a positive trigger.

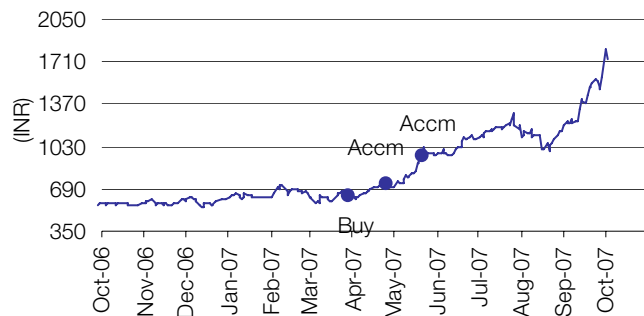
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### Coverage group(s) of stocks by primary analyst(s): Banking and Financial Services:

Allahabad Bank, Axis Bank, Centurion Bank of Punjab, Federal Bank, HDFC Bank, ICICI Bank, IOB, Karnataka Bank, OBC, SBI, Yes Bank, IDFC, HDFC, LIC Housing Finance, PNB, Power Finance Corporation, Reliance Capital, SREI Infrastructure Finance, Shriram City Union, Syndicate Bank and Union Bank.

### Reliance Capital



### Recent Research

Date	Company	Title	Price (INR)	Recos
01-Oct-07	<b>BFSI Update</b>	The butterfly effect; <i>Fortnightly Update</i>		
17-Sep-07	<b>Kotak Mahindra Bank</b>	At vantage point; <i>Initiating Coverage</i>	798	Buy
27-Aug-07	<b>Shriram City Union Finance</b>	Raring to go; <i>Initiating Coverage</i>	250	Buy
27-Aug-07	<b>BFSI Update</b>	Choppy fortnight; <i>Fortnightly Update</i>		

### Distribution of Ratings / Market Cap

#### Edelweiss Research Coverage Universe

	Buy	Accumulate	Reduce	Sell	Total
Rating Distribution*	100	46	23	6	183

\* 6 stocks under review / 2 rating withheld

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	83	66	34

### Rating Interpretation

Rating	Expected to
<b>Buy</b>	appreciate more than 20% over a 12-month period
<b>Accumulate</b>	appreciate up to 20% over a 12-month period
<b>Reduce</b>	depreciate up to 10% over a 12-month period
<b>Sell</b>	depreciate more than 10% over a 12-month period

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