

Not Rated

Target Price: NA*

CMP*	: Rs 1,820
Potential Upside*	: NA

MARKET DATA*

No. of Shares	: 130 mn
Market Cap	: Rs 235 bn
Free Float	: 37%
Avg. daily vol (6mth)	: 411,592 shares
52-w High / Low	: Rs 1,815 / Rs 1,047
Bloomberg	: ABNL IB Equity
Promoter holding	: 63%
FII / DII	: 12% / 9%

Aditya Birla Capital Ltd

(A SUBSIDIARY OF ADITYA BIRLA NUVO LIMITED (ABNL))

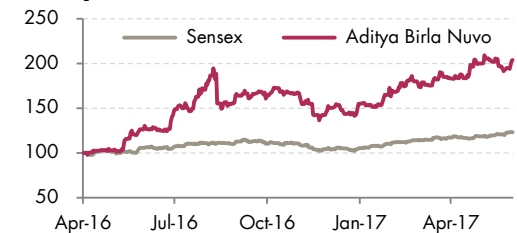
BANKS & FINANCIAL SERVICES

The next finance superstore

- NBFC
- Life insurance
- Housing finance
- Health insurance
- Insurance broking
- Private equity
- Wealth management
- Currency & commodity broking

*Note: All the above details refer to ABNL

Price performance*



*Note: Price chart refers to ABNL

Content

Aditya Birla Capital

BANKS & FINANCIAL SERVICES

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Company overview

Aditya Birla Capital

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Aditya Birla Nuvo (ABNL) will soon be merged with Grasim Industries, followed by demerger and listing of the group's financial services entity Aditya Birla Capital (ABCap). Shareholders of ABNL holding 100 shares will get 150 shares of ABNL-Grasim (which will hold 57.3% in ABCap post demerger) and 210 shares of ABCap. Grasim announced a 5:1 share split in Oct'16; the swap ratios above have been adjusted accordingly to take into account the effect of the split.

We met the top management teams of key business segments of ABCap to get an update on the businesses.

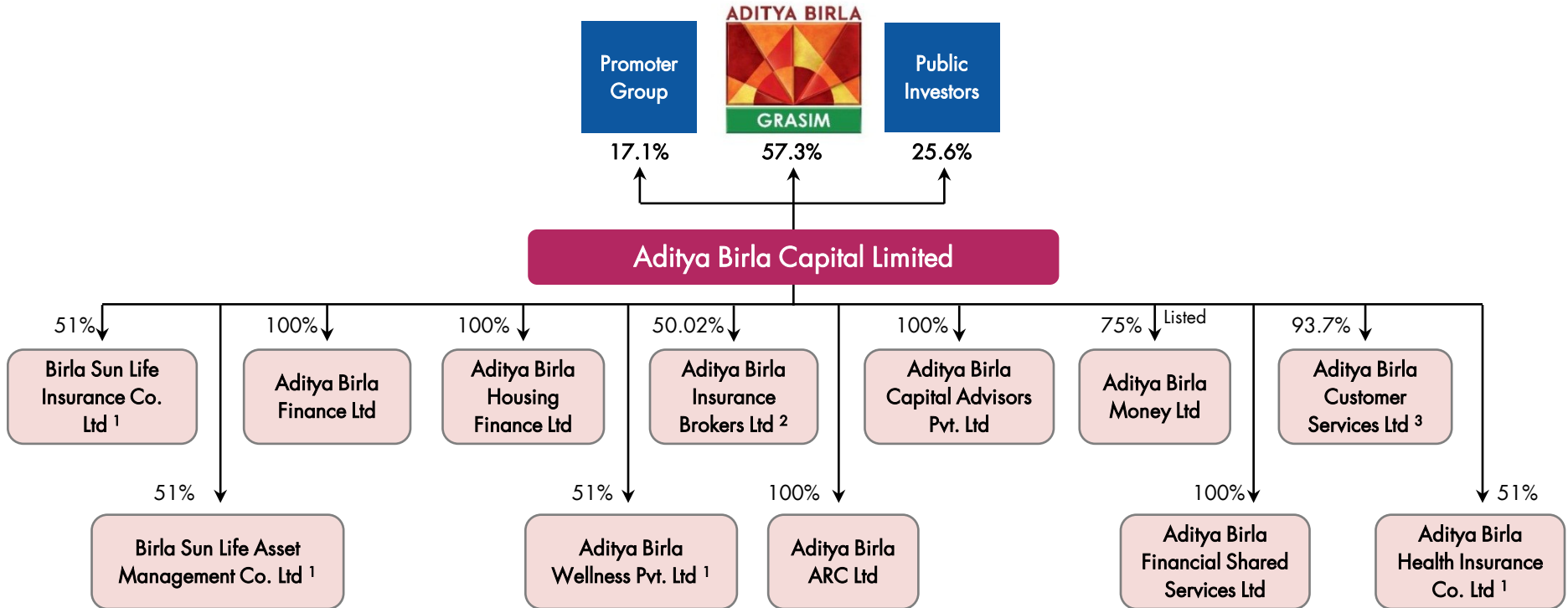
- ◆ ABCap is expected to be listed in August 2017 and will be one of the **premier finance superstores providing a play on 12 lines of financial services business** including:
 - **Credit** (corporate lending, project & structured finance, housing finance)
 - **Insurance** (life & health insurance, general insurance broking)
 - **Asset management** (AMC, private equity, wealth & pension management) and
 - **Other financial services** (online money management, retail broking etc). ABCap has also applied for a license with RBI to start asset reconstruction and securitization business
- ◆ ABCap has AUM of Rs 2.5 trn (incl. AUM of life/health insurance, PE & AMC; & lending book AUM of Rs 388 bn of NBFC/HFC business). FY17 consol revenue was ~Rs 58 bn & PBT ~Rs 10.7 bn (based on IGAAP financial statements of individual subs & JVs (consol accounts incl. 9 days of BSLI) before inter company adjustments & deduction of minority interest)
- ◆ **Financial services – Birla group's next flagship in the making:**
 - ABCap aims to be an end-to-end financial services provider catering to every finance need throughout the customer's lifecycle
 - The financing arms, ABFL and ABHFL, aspire to provide a majority of the products offered by any bank (excl. liabilities)
 - Focus is on being the leader in each business on the back of strong partnerships (partnered with Sun Life for life insurance and asset management businesses and MMI Holdings for health insurance)

NOTE: WE DO NOT HAVE COVERAGE ON ABCAP OR ABNL. At CMP of Rs 1,820, ABNL trades at 26x FY17 P/E and 1.4x FY17 P/BV

ABCap – Corporate structure

Aditya Birla Capital

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¹ Indicates JV. ² 49.998% of ABIBL is held by Infocyper India Pvt Ltd. ³ 6.3% of ABCSL is held by employee welfare trust (under ESOP)
 Note: ABCap structure contains major subsidiaries and excludes step down subsidiaries, if any Aditya Birla Money - Market Cap: Rs 3.7 bn

Businesses	ABFSL Stake (%)	Valuation basis	BEAR (Rs bn)	BASE (Rs bn)	BULL (Rs bn)	Comments
ABFL (NBFC)	100%	P/BV (FY19E)	193	215	268	~25% loan growth CAGR over the next 5 years with expected RoE of ~17-18% in 3 years. GNPA (FY17) < 0.5%; NNPA < 0.25% despite moving to 120 dpd
BSLI (Life Insurance)	51%	P/EV (FY17)	45	54	72	Listed and unlisted peers trade at 2.4x to 3.9x FY17 P/EV. Last deal 2 years ago valued the company at 73.5 bn, post which there has been significant improvement in business and tie up with HDFC Bank
BSLAMC (Mutual Fund)	51%	% OF AUM (FY17)	50	50	60	Most recent deals have valued AMC's at ~4-6% of AAUM. BSLAMC has doubled market share over past 5 years.
HFC (Housing Finance)	100%	P/BV (FY17)	11	18	18	AA+ rated company focused on Affordable Housing; High growth, Huge potential business. Operating leverage yet to play out as company in investment phase
Other Financial Services	100%	Invested Capital (FY17E)	0.8	0.8	1.3	Incl: Health Insurance, MyUniverse, Private Equity, Wealth Management, General Insurance Advisory (50%), Retail broking (75%)
Total equity value (Rs bn)			300	338	420	

- ◆ We do not have active coverage on ABNL or ABCap (yet to be listed). Instead we detail above, the likely scenarios and expected market cap
- ◆ The company has the option to sell 5% stake to strategic investors, which may provide benchmark valuations for eventual listing. As of 29th June 17, ~2.2% stake of the company has been sold by it, valuing it at Rs 320 bn (~Rs 145.4 per share)

ABCap's value ranges between Rs 300 bn and Rs 420 bn as per our current estimates

Corporate restructuring process

- ◆ **Merger of ABNL with Grasim Industries to form ABNL-Grasim (consolidated entity)**
 - Transfer of stake in BSLI from ABNL to ABCap (100% subsidiary of ABNL-Grasim which houses all financial services businesses) - **Completed on 23rd March 2017**
 - Demerger of Aditya Birla Capital from ABNL-Grasim into ABCap and separate listing of ABCap in such a way that Grasim will hold 57.3% stake in ABCap
(Rationale: ABNL is "AA+" rated, whereas Grasim is "AAA" rated, enabling easier and cheaper access to funds)

- ◆ **Share swap details**
 - Step 1: Each shareholder of ABNL to get 1.5 shares of ABNL-Grasim
 - Step 2: Each shareholder of ABNL-Grasim holding 5 shares will get 7 shares of ABCap (for demerger)

- ◆ So effectively, each shareholder of ABNL holding 100 shares will get
 - 150 shares of ABNL-Grasim (which will hold 57.3% in ABCap) and
 - 210 shares of ABCap upon its demerger from ABNL-Grasim

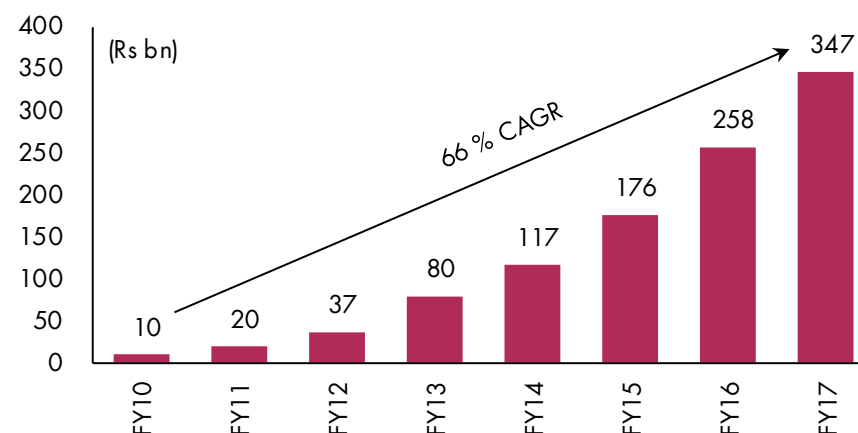
- ◆ Grasim had also announced a 5:1 share split in Oct 2016. The swap ratios above have been adjusted accordingly to take into account the effect of the split

Aditya Birla Finance (NBFC)

A diversified loan book firing on all cylinders

- ◆ Owing to the natural advantage of a small base, Aditya Birla Finance (ABFL)'s book has grown from ~Rs 10 bn as of FY10 to Rs 347 bn as of FY17, clocking a remarkable CAGR of 66%
- ◆ We believe ABFL would be able to continue to grow significantly above the industry and record ~25% CAGR over the next 5 years
- ◆ Growth would be driven by product expansion, larger share of SME and retail segments and expansion into new geographies
- ◆ The venture into unsecured lending (personal & business loans) and housing finance has emanated from this. We believe ABCap would grow unsecured business to as much as 10% of the book in the medium term (currently at ~2%)
- ◆ However, there are certain businesses where ABFL would not venture into like transaction banking, gold loans, two-wheeler and auto financing, either due to structural hindrances or cost of delivery

Loan book growth trend (%)



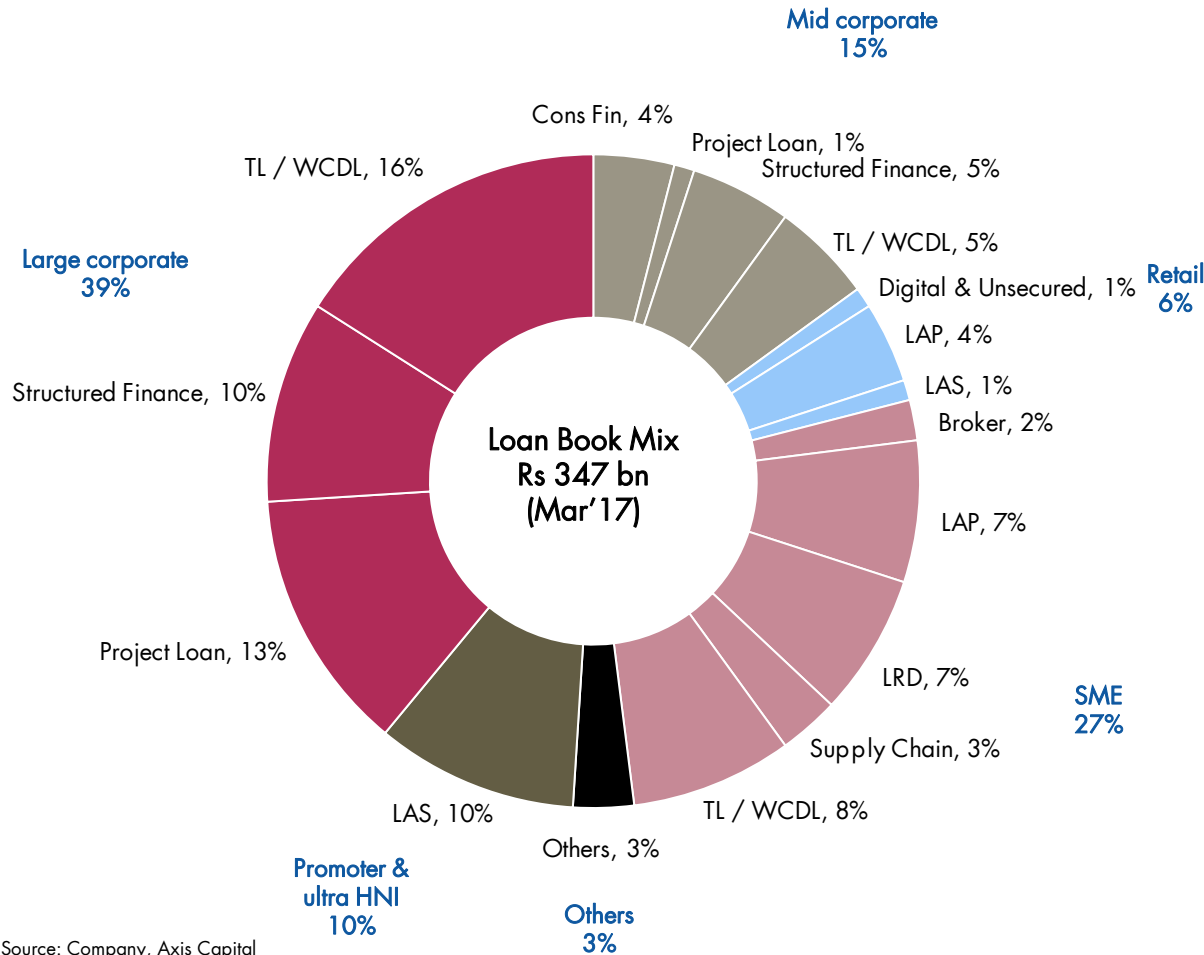
Product introduction history

In the past		FY12 - 13				FY14 - 17		Planned foray
Margin trade funding	IPO funding	Supply chain finance	Loan against property	Lease rental discount	Com. property purchase	Personal loans	Wealth management	Healthcare financing
Promoter funding	Loan against shares	SME lending	Project & structured finance	DCM	Builder finance	Digital lending	Unsecured business loans	Consumer durables financing
								Education loans

Source: Company, Axis Capital

Increasing diversification – a solution to growth stagnation

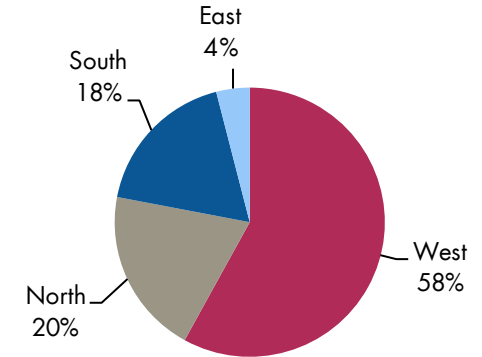
Loan book mix (%) FY17



Source: Company, Axis Capital

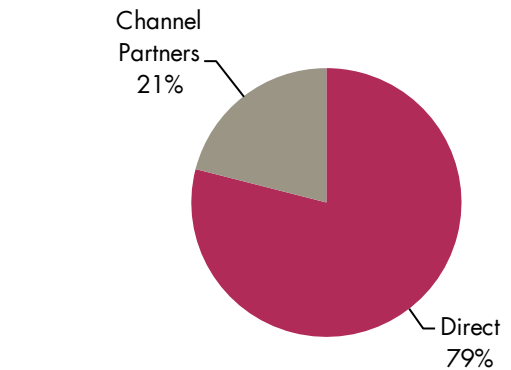
Note: Wealth management business merged with ABFL wef 1st April, 2016. Wealth AUA stood at Rs 135 bn as on 31st March 2017

Portfolio mix by geography (excl. wealth)



Source: Company, Axis Capital

Sourcing mix (excl. wealth)



Source: Company, Axis Capital

Robust risk-management framework, best in class credit quality

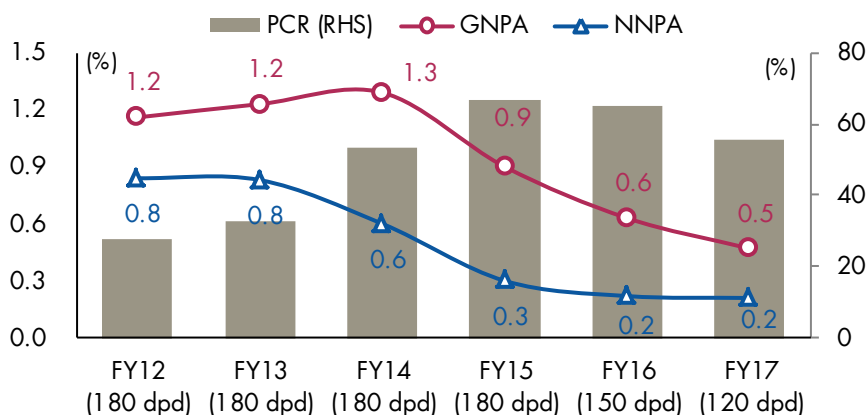
- ◆ ABFL has separate sourcing and underwriting teams for each business segment, which is derived from its **'one-shoe-fits-one'** philosophy of risk management.

It hires experienced top-level management to head any new product line that it ventures into.

- ◆ ABFL only lends to entities with strong promoter backing, and only to operating projects in the infra space. It does not do any form of green field financing in thermal power, or other such long-gestation projects (except renewable energy)
- ◆ As a result of this, ABFL's asset quality has been pristine, with GNPA's of ~0.5% on 120 dpd in FY17, despite high growth rates

- ◆ In the large corporate book, there is no restructured accounts and no account which is even 0 dpd
- ◆ Average internal rating is A+

Trend in GNPA and NNPA (%)



Source: Company, Axis Capital

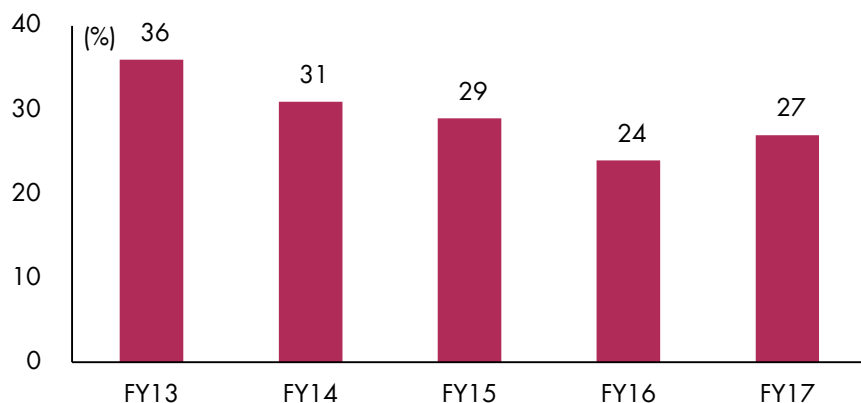
- ◆ Infra book finances mostly operating projects (~95%+)
- ◆ Except for under-construction renewable energy projects (incl. hydro projects) (~6% of total loans) which are by-default rated BBB at best, all infra/structured finance loans are to entities rated A or above
- ◆ Inherent advantage of smaller base allows for rapid growth without lending to sub-par promoter groups

Improving profitability, return ratios

- ◆ Management is confident of controlling Cost to Income (CI) ratio in long run as
 - investments on the digital side wane and
 - business continues scaling up, deriving operating leverage.

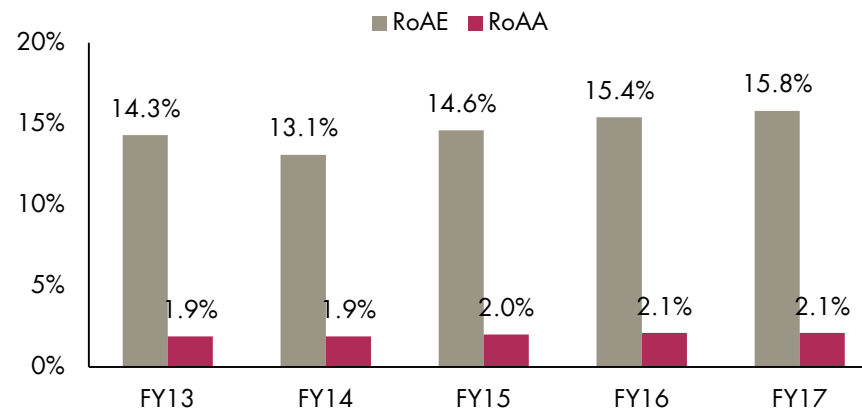
- ◆ We believe AB Cap can achieve better returns ahead given:
 - Higher share of SME and retail book (from 33% now to 50% in ~3 to 5 years) as indicated by management
 - Higher share of unsecured retail loans (from ~2% now to ~10% in ~3 years) &
 - Investments in digital lending bearing fruit (lower incremental opex)

ABFL – Opex to Net Interest trend (%)



Source: Company, Axis Capital

Trend in return ratios (%)



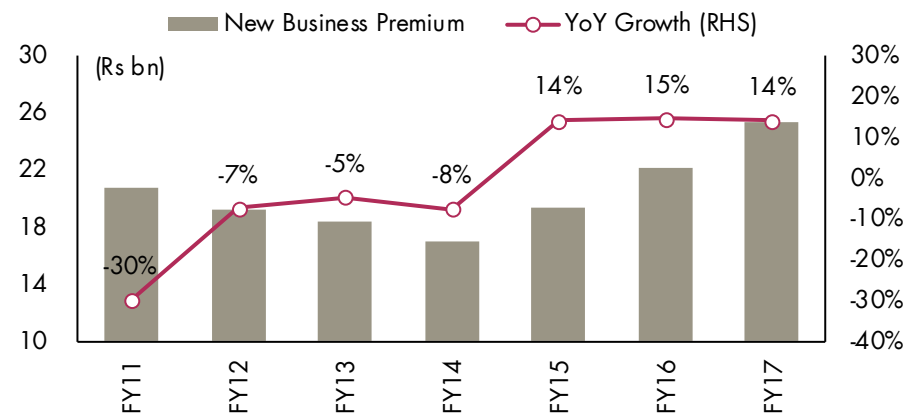
Source: Company, Axis Capital

Birla Sun Life Insurance

Retreat – ULIP regulations hurt growth, profitability

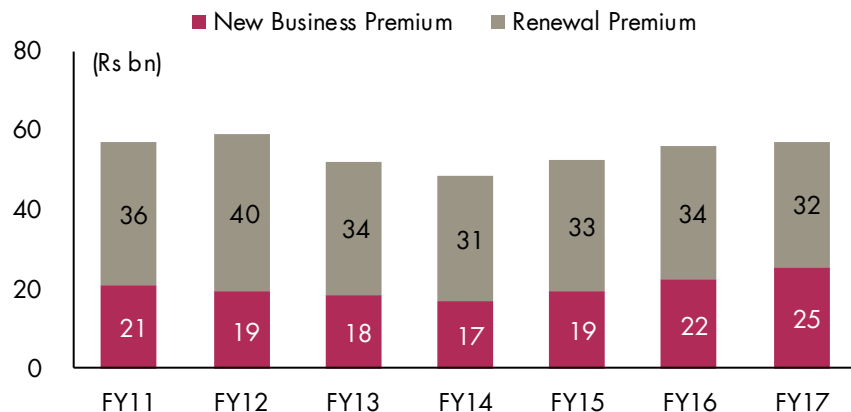
- ◆ Birla Sun Life Insurance (BSLI) is a JV between ABCap and Sun Life Insurance (Canada) and is amongst the top private insurers in the country
- ◆ BSLI was primarily focused on ULIP policies, with almost 100% of new premiums sourced from ULIP policies in FY10. However, the ULIP regulations in 2010 nearly caused an existential crisis for the company
- ◆ Premium de-grew and embedded value (from Rs 41 bn in FY10 to Rs 34.3 bn in FY17) and profitability (NBAP margin declining from 27.5% in FY11 to 17% in FY17) slid

Trend in new business premium (%)



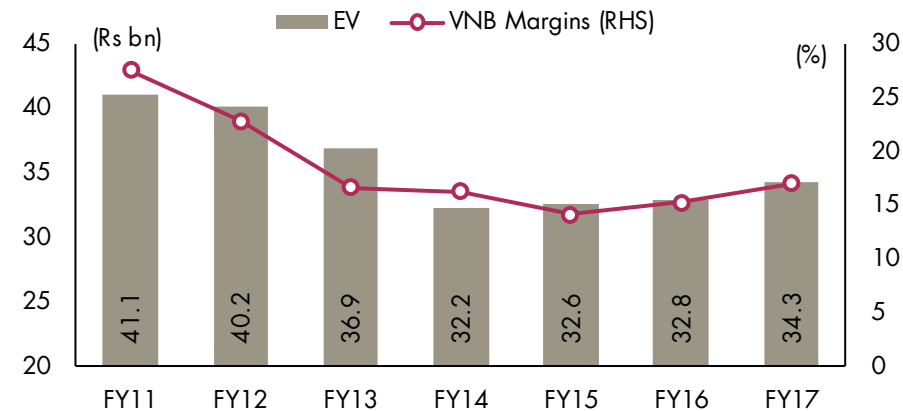
Source: Company, Axis Capital

Total premium has stagnated over past few years



Source: Company, Axis Capital

Trend in EV (traditional) and NBAP margin (pre-over run)

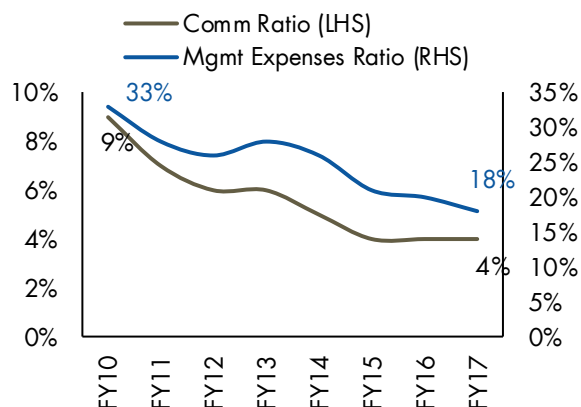


Source: Company, Axis Capital

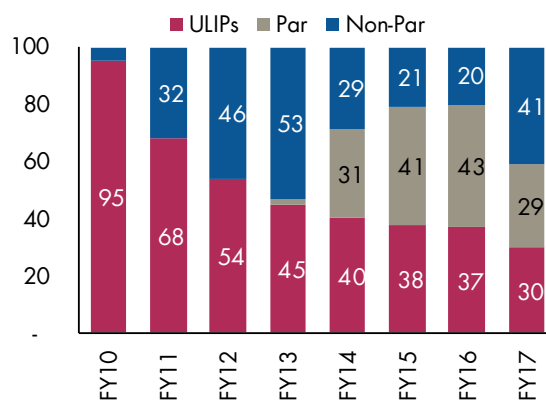
Recoup – Business reorganized

- Following the IRDA ULIP regulations, BSLI (which had nearly 100% of its new business coming from ULIPs in 2010) underwent a prolonged and grueling consolidation between FY10-14. This saw its new business premium growth turn negative during the period
- However, this may have been a blessing in disguise, and the company has emerged stronger and more focused

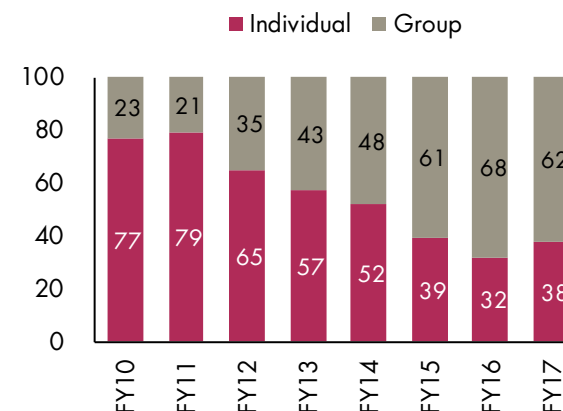
Trend in expense ratios



Business mix – Individual (%)



Business mix - Total (%)



BSLI controlled costs and curbed profitability deterioration, as is evident from the 15 ppt decline in management expense ratio over FY10-17

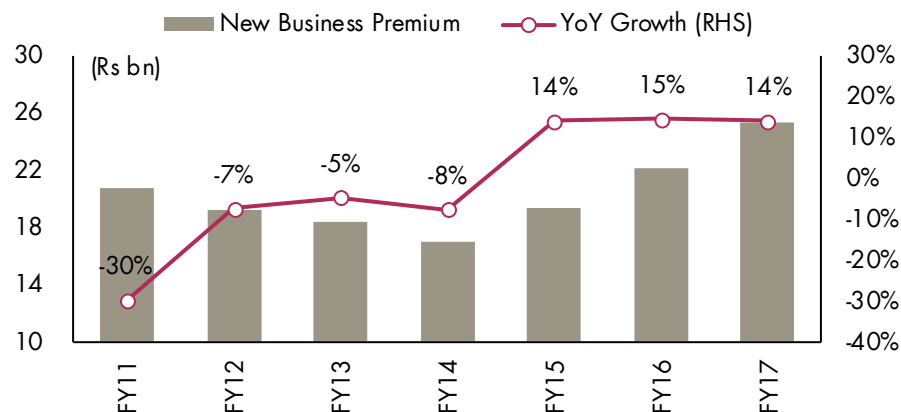
It adopted a balanced product approach, with all 3 types of products contributing equally. ULIPs constituted only 30% of premiums in FY17 vs. almost 100% in FY10

Absence of a strong Banca partner has been hurting distribution, and hence premium mix has shifted towards group business (62% contribution in FY17)

Source: Company, Axis Capital

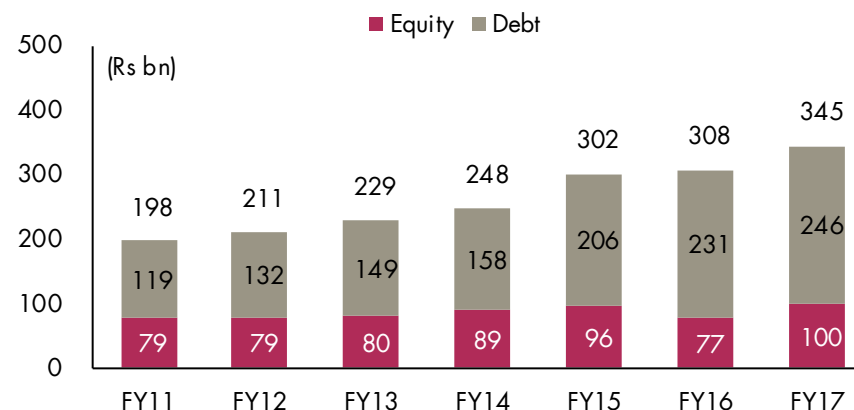
Rejuvenate – Back on growth path

New Business Premium de-growth reversed in FY15, with new business CAGR of 14% in past 3 years



Source: Company, Axis Capital

AUM crossed Rs 345 bn



Source: Company, Axis Capital

BANCASSURANCE TIE-UP WITH HDFC BANK – A BIG BOOST



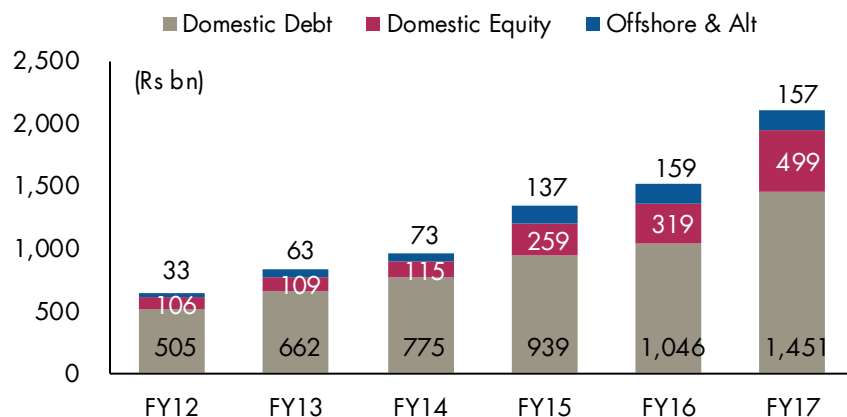
- ◆ Under the new open architecture rules of IRDAI, banks are allowed to tie up with up to 3 insurance companies each in life, general & health insurance
- ◆ In the first such move, BSLI through its strong parentage and influence secured Banca partnership with HDFC Bank – the largest private sector bank in India
- ◆ This provides BSLI access to the distribution network of a premiere bank. We believe BSLI can double its growth rate even if it garners ~10% share of policies which are sold by HDFC Bank
- ◆ Current banca partners: LVB, DCB Bank, Deutsche Bank, Karur Vysya Bank, DBS Bank

Other key businesses

Asset management (BSLAMC) – Maintaining its dominance

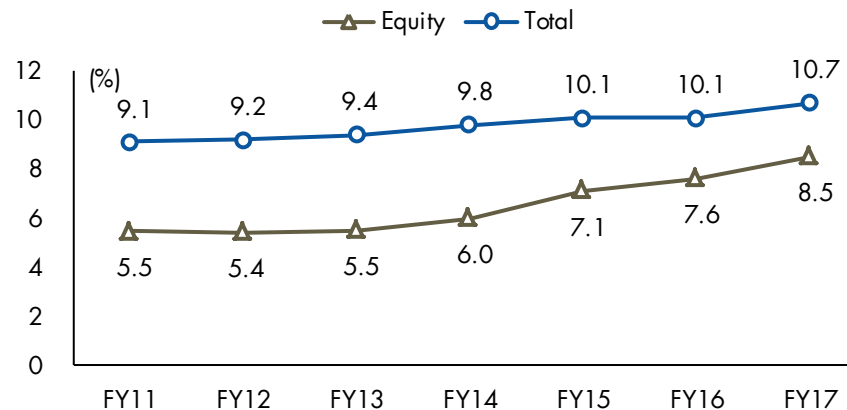
- ◆ BSLAMC is among the **top 4 AMC**s in India and has a domestic AAUM market share of ~10.7%. Its AAUM increased at ~26% CAGR over FY13-17 at Rs 2.1 trn
- ◆ With a **fixed income AUM of more than Rs 1.4 trn** as of FY17, it enjoys a dominant position in the segment with market share of ~12%. On equity front too it has sharply gained market share in the segment (up ~300 bps in past 4 years) and **manages equity funds of ~Rs 500 bn**
- ◆ It posted PBT of Rs 3.4 bn in FY17 on strong growth in AUM and increasing contribution of higher fee generating equity AUM
- ◆ Management will focus on shoring up **retail equity AUMs**, which tend to be stickier, and help achieve granularity in client base. The SIP book has grown at 55% CAGR over FY13-17 and now stands at Rs 5 bn per month

AUM mix trend



Source: Company, Axis Capital

Steady market share gain in all segments

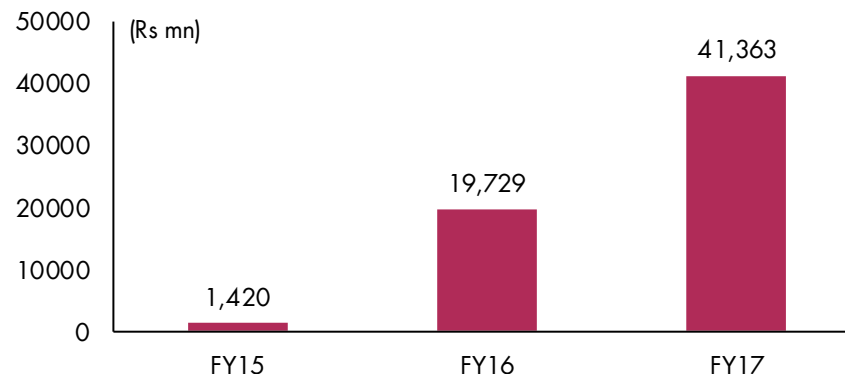


Source: Company, Axis Capital

Housing Finance (ABHFL) – Significant opportunity

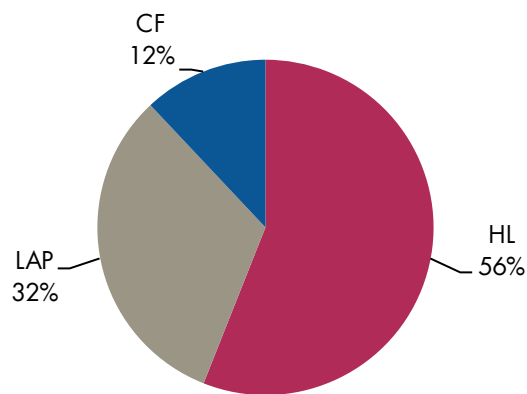
- ◆ ABHFL commenced operations in FY15 and has quickly grown to a book size of Rs 41 bn as of FY17. It is present through its ~40 branches and targets 60 branches in FY18
- ◆ Average ticket sizes in housing loan business will trend down with expansion into smaller geographies
- ◆ Management expects C/I to remain elevated for few more years as the company is still in investment phase
- ◆ Large pool of internal customers and stakeholders/ dealers etc. in group businesses are low-hanging fruit for this business

Sput in lending book on a small base



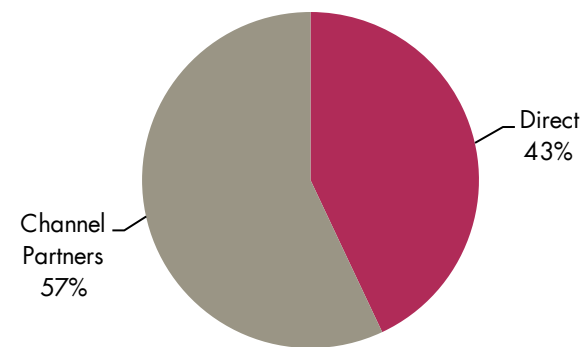
Source: Company, Axis Capital

Product composition – FY17



Source: Company, Axis Capital

Sourcing mix – FY17



Source: Company, Axis Capital



Health Insurance (JV with MMI Holdings) – operations commenced

- ◆ Favorable demographics (young populace, increasing awareness and increasing affordability) make the business lucrative (industry growing at ~18% p.a.)
- ◆ Despite being a late entrant, can leverage strong brand name to grow comfortably
- ◆ Partnership with MMI will help launch differentiated and first-in-India products (money back, wellness premium, pre-existing disease coverage)



Aditya Birla Insurance Brokers Limited (ABIBL)

- ◆ Leading general insurance advisory player
- ◆ In FY17, ABIBL's revenue rose ~25% YoY to Rs 1.2 bn outpacing the industry average growth of 14%, resulting in market share gains from 1.7% to 2.0%

Other financial services businesses

Aditya Birla Capital

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Other businesses

- ◆ Private equity – PE Funds under management (net) at ~Rs 8 bn as of FY17 (gross funds ~Rs 11.8 bn)
- ◆ Wealth management – Assets under advisory at Rs 135 bn as of FY17
- ◆ Online money management – through the MyUniverse platform with 3.76 mn users and servicing funds exceeding Rs 205 bn

Company financials – ABNL

Aditya Birla Capital

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Consolidated Profit & Loss Account

(Rs mn)	Full Year	
	FY16	FY17
Revenue	133,150	145,770
EBITDA	30,600	39,260
Less : NBFC Interest expenses	16,000	22,760
Less : Other Interest Expenses	2,790	2,180
EBDT	11,810	14,320
Less : Depreciation	1,730	2,040
Earnings before Tax (before exceptional items and share of profit/(loss) of associates and Joint ventures)	10,080	12,280
Share of Profit / (loss) of associate and Joint ventures	7,530	110
Exceptional Gain / Profit attributable to discontinued operations	4,110	160
Earnings before Tax	21,720	12,550
Less : Provision for Taxation (Net)	5,320	2,980
Less : Minority Interest	270	490
Net Profit	16,130	9,080

Source: Company, Axis Capital

Losses in Idea Cellular drag down share of profit/(loss) of associate and JVs

Exceptional gains in FY16 largely due to demerger of Pantaloons Fashions and resultant reversal of losses

Company financials – ABNL

Aditya Birla Capital

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Consolidated Balance Sheet

(Rs mn)	FY16	FY17
Net Worth	133,910	163,170
Minority Interest	4,920	10,950
Debt	39,400	34,080
NBFC borrowings (incl. Housing)	234,880	328,650
Deferred Tax Liabilities (Net)	7,340	5,890
Capital Employed	420,450	542,730
Policyholders' funds (Incl. funds for future appropriation)	302,450	343,340
Total Liabilities	722,900	886,070
Net Block (Incl. Capital Advances)	17,410	19,780
Goodwill on Consolidation	2,630	2,630
NBFC Lending (Incl. Housing)	277,280	388,390
Net Working Capital	14,190	8,720
Long Term Investments	93,360	102,170
Insurance Investments	310,620	350,210
Cash Surplus & Current Investments	7,410	14,160
Total Assets	722,900	886,070
Key Ratios	FY16	FY17
Book Value (Rs)	1,028	1,253
Net Debt / Annualised EBITDA (x)	2.2	1.2
Net Debt / Equity (x)	0.24	0.12

Source: Company, Axis Capital

Lending book grows at 35% YoY, driving balance sheet growth

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DEFINITION OF RATINGS	
Ratings	Expected absolute returns over 12 months
BUY	More than 10%
HOLD	Between 10% and -10%
SELL	Less than -10%

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