# Motilal Oswal Financial Services

## ConCall Summary & Earnings Release

### Quarter ended Sep 2017

06 Nov 2017

Motilal Oswal Financial Services Limited (MOFSL) posted consolidated revenues of Rs 7.1 billion for Q2FY18, +35% YoY. PAT was Rs 1.4 billion for Q2FY18, +42% YoY. Broking-related revenue was Rs 2.2 billion in Q2FY18, +21% YoY. Asset management revenue was Rs 2.5 billion in Q2FY18, +61% YoY.. Housing finance-related revenue was Rs 1.8 billion in Q2FY18, +22% YoY. Investment banking income was Rs 0.2 billion in Q2FY18, +9% YoY. Fund-based revenue was Rs .4 billion in Q2FY18, +86% YoY.

For a deeper insight into the company's performance and the management's expectations, we present extracts from the post-results conference call. We have edited and rearranged the transcript for greater lucidity. We have also included exhibits from the company's presentation on its performance for the quarter ended Sep 2017. This presentation is available at www.motilaloswalgroup.com

**Corporate Participants**

Mr Motilal Oswal

*Chairman*

Mr Raamdeo Agrawal

*Joint Managing Director*

Mr Navin Agarwal

*Managing Director*

Mr Shalibhadra Shah

*Chief Financial Officer*

Mr Rakesh Shinde

*Investor Relations*

This document includes forward looking statements, including discussions about the management's plans and objectives and about expected changes in revenues and financial conditions. Forward-looking statements about the financial condition, results of operations, plans and business are subject to various risks and uncertainties that could cause actual results to differ materially from those set forth in this document. You should not construe any of these statements as assurances of financial performance or as promises of particular courses of action.

Welcome to the 2nd Quarter of FY18 Earnings Conference Call for Motilal Oswal Financial Services Limited. We have with us today Mr. Motilal Oswal-Chairman, Mr. Raamdeo Agrawal-Joined Managing Director, Mr. Navin Agarwal-Managing Director, Mr. Shalibhadra Shah-Chief Financial Officer and Mr. Rakesh Shinde-Investor Relations. For the duration of the presentation all participant lines will be in the listen-only mode. I will be standing by for the question and answer session. I would now like to invite Mr. Navin Agarwal to make his opening remarks. Thank you and over to you sir…

**MOFSL CONSOLIDATED FINANCIALS (Rs Mn)**

| Particulars | Q2 FY18 | Q2 FY17 | CHG. YoY | Q1 FY18 | CHG. QoQ | H1 FY18 | H1 FY17 | CHG. YoY | FY17 |
|---|---|---|---|---|---|---|---|---|---|
| **Total Revenues** | **7,144** | **5,285** | **35%** | **5,761** | **24%** | **12,905** | **9,298** | **39%** | **19,315** |
| EBITDA | 3,713 | 2,766 | 34% | 2,739 | 36% | 6,452 | 4,934 | 31% | 10,182 |
| Exceptional items | 0 | -79 | nm | 0 | nm | 0 | -279 | nm | -279 |
| PBT | 2,314 | 1,486 | 56% | 1,386 | 67% | 3,700 | 2,549 | 45% | 5,152 |
| **PAT** | **1,438** | **1016** | **42%** | **1,016** | **42%** | **2,454** | **1807** | **36%** | **3,600** |
| EPS - Basic | 10 | 7 | | 7 | | 17 | 13 | | 25 |
| EPS - Diluted | 10 | 7 | | 7 | | 17 | 13 | | 25 |
| Shares O/S (mn) - FV | 145 | 143 | | 144 | | 145 | 143 | | 144 |

**REVENUE COMPOSITION (Rs Mn)**

| Particulars | Q2 FY18 | Q2 FY17 | CHG. YoY | Q1 FY18 | CHG. QoQ | H1 FY18 | H1 FY17 | CHG. YoY | FY17 |
|---|---|---|---|---|---|---|---|---|---|
| Brokerage | 2,193 | 1,806 | 21% | 1,977 | 11% | 4,169 | 3,164 | 32% | 6,396 |
| Investment banking | 220 | 202 | 9% | 230 | -4% | 451 | 284 | 59% | 855 |
| Asset management | 2,549 | 1,583 | 61% | 1,498 | 70% | 4,048 | 2,671 | 52% | 5,102 |
| Fund based income | 361 | 194 | 86% | 422 | -14% | 783 | 652 | 20% | 1,174 |
| Housing finance | 1,804 | 1,482 | 22% | 1,600 | 13% | 3,404 | 2,484 | 37% | 5,705 |
| Other income | 16 | 19 | -17% | 35 | -55% | 50 | 42 | 19% | 82 |
| **Total Revenues** | **7,144** | **5,285** | **35%** | **5,761** | **24%** | **12,905** | **9,298** | **39%** | **19,315** |

## Opening remarks

Good afternoon. It is my pleasure to welcome all of you to the Motilal Oswal Financial Services earnings call for the 2nd quarter of FY18. The quarter and half year ended Sep-17 marks meaningful progress towards the strategic objective outlined a few years ago to achieve business model offering greater linearity and higher Return on Equity. The strong growth reported in the past several quarters have come from different businesses across quarters ranging from Asset Management, Home Finance, Retail and Institutional Broking, Private Equity, Investment Banking and Wealth Management, testimony to the diversity in business model. We are excited by the overall positioning of each of these 7 businesses to capitalise on the various tailwinds created by financialisation of savings, shift from unorganised to organised due to de-monetisation and GST and several other macro trends. We reported our highest revenues and profits for a quarter and half year during this year. Revenues grew 35%, PBT grew 56% and PAT grew 42% YoY. RoE scaled up to 29% and to 32% including unrealised gains despite modest gearing ex-Aspire and very strong liquidity in the balance sheet. Headroom to grow in each of our businesses remains enormous driving us to make significant investments in manpower, technology, branding and network building. Management remains fully committed to staying sharply focused on the existing 7 businesses, deepening the moats in each of these businesses, scaling them to their potential and extracting operating leverage that the journey offers.

Our consolidated revenues in Q2FY18 stood at Rs 7.14 bn, +35% YoY. Asset & Wealth Management business topline was +61% YoY, Housing finance +22% YoY and capital markets +20% YoY. 61% of revenue in Q2FY18 came from linear sources like Asset & Wealth Management and Housing Finance. While the share of Capital Markets continued to fall to 34%, it also continued to report topline growth on 20% and bottom-line growth of 34%. In fact, Broking business has clocked its highest ever quarterly revenues and profits, its distribution arm clocked 130% YoY growth in AUM and Investment banking profits and pipeline continued to grow strongly. Notwithstanding this strong performance in Capital Markets, the share of annuity revenue streams went up, led by AMC's AUM growth of 92% YoY and Housing Finance business reporting a loan book growth of 57% YoY.

**Consolidated PBT was up by 56% YoY at Rs 2.31 bn**.

**Consolidated PAT** was Rs 1.44 bn in Q2FY18, +42% YoY, despite the impact of MAT credit provisioning of Rs 149mn. This incremental PAT growth was contributed by Asset & Wealth Management business, +52% YoY, followed by Capital Market business, +38% YoY and fund based business. In fact, Profits of AMC alone grew by 154%. Significant investments have been made in headcount, which is up 44% in Retail broking and 70% in Housing finance. Ad expenses are +51% YoY in Asset Management. In case of Housing Finance, branches are up by 62% YoY. The full impact of operating leverage from these sizeable investments is yet to unfold in most of these businesses.

**Consolidated net worth** has crossed Rs 20 bn mark, gross borrowing was Rs 55 bn and net borrowing was Rs 52 bn (including Aspire). Excluding Aspire, gross and net borrowings were Rs 15 bn and Rs 12 bn respectively. Against this borrowing, balance sheet has strong liquidity, with ~Rs 13 bn in near-liquid investments as of

Sep-17 to fund any future investment needs of operating businesses. RoE for Q2FY18 was 29% on the reported PAT. However, this does not include unrealized gains in our quoted investments at Rs 5.8 bn as of Sep-17. Had this been included, RoE in Q2FY18 would have been ~32%.

**1. Capital Market Businesses**

- Capital markets comprises of Retail Broking, Institutional Equities and Investment Banking business. Revenues were Rs 2.4 bn in Q2FY18, +20% YoY for this segment and ~34% of Cons revenues while profits grew much faster at 38% YoY, contributing to ~29% of PAT.
- In **Retail Broking & Distribution**, our market share in high-yield cash segment continued to rise QoQ and overall market share improved to 2% in Q2FY18.
- Our strategy to bring in linearity through the trail-based distribution business is showing results. Distribution Net Sales were Rs 8.2 bn in Q2FY18, +142% YoY, and AUM was Rs 61 billion, +130% YoY. With only 9% of the near million client base tapped Distribution income at 15.9% of retail broking net revenues. We expect a meaningful increase in AUM and fee income as number of clients to whom we have cross sold and number of products per client cross sold rises.
- In **Institutional Broking**, blocks continued to gain solid traction within our volumes, rankings with existing clients improved, domestic institutions contribution improved and new client additions were encouraging at 15 adds during the quarter. Every aspect of the business, research, sales, sales trading and corporate access is being strengthened. Tailwinds for local firms are strong notwithstanding headwinds of muted FII investments, falling commissions and unbundling.
- **Investment Banking** revenues grew strongly by 59% YoY to Rs 465 mn in H1FY18 while profits grew much faster. Our IB was among the top 10 investment banks in primary market equity deal ranking in H1CY17. It has completed 7 ECM transactions in H1FY18. Some significant transactions have already been close in Q3FY18 and the overall transaction pipeline remains quite encouraging.

**2. Asset and Wealth management**

- **Asset Management** business across MF, PMS & AIF reached the mark of Rs 290 bn AUM, +92% YoY this year, comprising of Rs 143 bn MF AUM and Rs 134bn PMS AUM. Our AMC now ranks among the Top-10 players by total equity assets, PMS ranks #1 while AIF is growing rapidly. Net Sales were Rs 61 bn in H1FY18, +141% YoY and compares with Rs 62 bn in all of FY17. Net yield was ~0.9% in Q2FY18. Revenues were Rs 1.46 bn in Q2FY18, +96% YoY and PAT is Rs 233 mn, +154%

YoY despite significant investments in brand building. The asset management business offers the highest scalability and operating leverage among all our businesses.

- Our mutual funds and PMS products are guided by QGLP philosophy and continued to deliver strong absolute returns and alpha over long periods of time. Our largest MF product by AUM, F-35, delivered absolute returns of 31% and alpha over benchmark of 16%, since inception. Our longest-running Value PMS delivered absolute returns of ~25% CAGR in 14 years. Our 3 flagship mutual funds schemes completed their 3-year performance track record, leading to increased participation from distributors.
- Our Equity MF AUM of Rs 143 bn is just 1.8% of the Industry Equity AUM of Rs 8 tn. However, our market share in Equity MF Net Sales has further scaled up to ~4.3% in Q2FY18. Our endeavor would be sharpen the QGLP philosophy to sustain alpha generation, to increase our share of Net Sales as funds form part of league tables and there is stronger distribution pull, and close the gap between our share in AUM and Net Sales as our vintage improves. Ad & marketing spends were Rs 85 mn in Q2FY18, +51% YoY and 85% QoQ, forming 14% of net revenue. Our ongoing ad campaign "Think Equity Think Motilal Oswal" is reiterating our positioning as equity specialist and has won the award for the best ad campaign in BFSI space. This addresses the unique challenge of gaining materiality in a market that is witnessing staggering growth. Separately, our pricing power in MF is improving and the direct net sales contribution is rising – up from 13% in Q2FY17 to 30% in Q2FY18. This will help improve net yields. We are also well positioned in the context of SEBI guidelines on scheme categorization and rationalization.
- Our share of Alternate assets, comprising of PMS & AIF, is the highest among AMC's at 50% and continues to grow very strongly. Yields and profitability of Alternates is higher. As of Sep 2017, ~15% of Alternates AUM is performance-fee linked, and our target is to increase this further.
- Financial savings to total savings in India has increased drastically although the share of financial assets in overall Household assets remain minuscule, making us believe that the shift is structural.
- AUM of FIIs in India is Rs 25 tn, over 3x of the size of MF AUM's. Our AMC has zero share of this segment as of now. Our QGLP philosophy is relevant to address this segment well and we are seeing initial interest in our offshore products.
- **Private Equity** manages an AUM of Rs 42 bn across 3 growth capital PE funds & 3 real estate funds. This business has delivered on profitability and scalability fronts. The 1st growth fund (IBEF 1) has delivered an XIRR of 29%, and alpha of 10% and is expected to return nearly 5x MoC (Multiple of Cost). Till date, 2.5x MoC has been

returned for INR investors and 2.2x for USD investors. The steady stream of exits at high IRRs across the 6 funds will bring some linearity to this income stream over the coming years. Strong performance and positioning has aided new fund raise. We launched IBEF-3 in 2QFY18 and received phenomenal response by garnering 10bn and are expected to close FY18 with corpus of Rs 20 bn.

- **Wealth Management** business AUM grew by 51% YoY at Rs 129 bn with highest-ever Net adds at Rs 9.1 bn, +91% YoY, revenues grew 51% YoY and PAT grew 151% YoY. EBITDA margins were 41% in 2Q & 38% in in 1H vs 31-33% in FY15-FY17. RM count of this business has doubled to 98 from 78 in Mar-17 and 49 in Mar-15. Investments in strong RM addition suppressed reported profitability of past years. As the ratio of new adds to opening RM's falls and the vintage of RM's improve, both productivity and profitability of the business will scale up.
- Overall **Asset and Wealth Management** revenues were Rs 2.5 bn in Q2FY18, +61% YoY and contributed 36% of consolidated revenues. Profits grew by 52% YoY and this segment now contributes 50% of Consolidated profits, with highest scalability and with least capital employed among our portfolio of businesses.

**3. Housing Finance business:-**

- **Aspire Home Finance** continues to deliver on growth, our loan book grew by +57% YoY at Rs 48 bn. NII of AHFCL grew by 75% YoY on account of lower interest expenses driven by lower borrowings and lower cost of funds during the quarter. This, coupled with further equity infusion in 1Q, drove margins from 4% to 4.5%. Profit for AHFCL was stable on YoY basis at Rs 223 mn. This was on account of higher expenses, +41% YoY coupled with higher provisioning during the quarter.
- Strong ramp in FY17 has driven 70% YoY growth in manpower and 62% growth in branches. However, YTD growth in manpower is 19% with no additions to branches. We have maintained steady operating metrics with average ticket-size of Rs 0.90 million, LTV of ~58% and FOIR of ~46%.
- Disbursements in Q2FY18 were Rs 6.3 bn versus Rs 3.3 bn in Q1FY18 and Rs 6.7 bn in Q2FY17. Calibration in the pace of disbursements in H1FY18 is a result of a combination of self-restraint and external factors that have caused postponement in customer decisioning.
- GNPA increased from 1.6% in Q1FY18 to 2.8% in Q2FY18 on account of seasoning of the book coupled with external shocks such as demonetization, RERA and GST. Also, in the first three years, there was no independent collection organization with collections being the responsibility of sales and credit, resulting in higher slippages. Investments have been made in building an independent collection and legal organisation while calibrating growth. This will create a strong foundation for

sustainable growth.

- Average cost of borrowing declined from 10% in Q2FY17 to 9.8% in Q2FY18 and could have been much lower but for the negligible CP contribution in funding mix. Incremental borrowings from CP will bring down cost of borrowings in H2FY18 YoY and HoH.
- RoA was 1.7% and RoE was 11.6% for Q2FY18. Though return ratios have improved sequentially, they are muted as compared to Q2FY17, led by slowdown in disbursements, significant investments in manpower (from 735 count to 1,246 YoY), branches and technology driving C/I from 37% to 41% YoY, higher provisioning cost and equity capital infusion of Rs 1 bn in Jun-17. Gearing also remains conservative, with the Debt/Equity ratio at 5.1x

**4. Fund based Business focuses on enhancing Return on Equity**

- Fund Based activities like commitments to our asset management products, not only helped seed these new businesses by investing in highly scalable opportunities, but they also represent liquid resources for future opportunities
- Investments in our mutual funds and listed securities stood at Rs 6.7 bn at cost, while the unrealised gain on these investments as of Sep-17 stood at Rs 5.8 bn. These gains are not reflected in the reported PAT. The post-tax cumulative XIRR of these investments is ~29%, which is the see-through RoE vs reported RoE of just 4%. As per IND-AS, these gains will form a part of reported earnings from the next fiscal year, FY19.
- Investment in seeding our PE funds is Rs 2.9 bn at cost. IBEF-1 is expected to deliver a 5x MoC. NBFC LAS book is Rs 2.24 bn as of Sep-17, which is now run as a spread business

**Outlook**

To sum up, our strategy of diversified business model towards linear sources of earnings is showing definite results with 56% PBT growth and 42% PAT growth during the quarter. All our 7 businesses continue to grow strongly, make significant investments, are building scale and offer meaningful operating leverage. Our brand is now being recognized in each of our businesses. RoE is best in class at 29% and 32% including unrealised gains. We remain excited about the headroom to grow in our existing businesses with several structural tailwinds and remain sharply focused on deepening moats in these businesses. We are now open for Q&A!

## 1. Capital Market Businesses

### Retail Broking & Distribution, Institutional Broking

**KEY FINANCIALS: MOSL (Rs Mn)**

| Particulars | Q2 FY18 | Q2 FY17 | CHG. YoY | Q1 FY18 | CHG. QoQ | H1 FY18 | H1 FY17 | CHG. YoY | FY17 |
|---|---|---|---|---|---|---|---|---|---|
| Total Revenues | 2,463 | 1,877 | 31% | 2,409 | 2% | 4,872 | 3,382 | 44% | 7,197 |
| EBITDA | 805 | 569 | 42% | 725 | 11% | 1,531 | 1,068 | 43% | 2,275 |
| PBT | 528 | 349 | 51% | 489 | 8% | 1,017 | 665 | 53% | 1,429 |

**In private sector banks, where the cost reduction in terms of realignment of employee base. In retail broking, major cost is employee cost. When the digitalization and the technology takes the central stage, how do you see that thing to pan out in our operation and our overall cost-to-income ratio in the medium term?**

There are two major businesses which are retail centric, one is broking business and second is housing finance business where you got highest number of employees, but we are putting lot of efforts on digitalization and digitalization of lot of processes. Another thing is offering leverage also you get because of the size. So we are not concerned about the rising cost either on the employee perspective or on the kind of digitalization. We feel that operating leverage should work along with the cost saving from digitalization.

### Investment Banking

**KEY FINANCIALS: INVESTMENT BANKING (Rs Mn)**

| Particulars | Q2 FY18 | Q2 FY17 | CHG. YoY | Q1 FY18 | CHG. QoQ | H1 FY18 | H1 FY17 | CHG. YoY | FY17 |
|---|---|---|---|---|---|---|---|---|---|
| Total Revenues | 225 | 202 | 11% | 240 | -6% | 465 | 293 | 59% | 872 |
| EBITDA | 180 | 82 | 120% | 167.430656 | 8% | 348 | 121 | 187% | 561 |
| PBT | 179 | 81 | 122% | 167.072638 | 7% | 346 | 118 | 194% | 554 |
| PAT | 128 | 51 | 153% | 147.772903 | -13% | 276 | 83 | 234% | 372 |

## 2. Asset & Wealth Management Businesses

### Asset Management

**KEY FINANCIALS: ASSET MANAGEMENT (Rs Mn)**

| Particulars | Q2 FY18 | Q2 FY17 | CHG. YoY | Q1 FY18 | CHG. QoQ | H1 FY18 | H1 FY17 | CHG. YoY | FY17 |
|---|---|---|---|---|---|---|---|---|---|
| AUM (Rs bn) | 289 | 150 | 92% | 242 | 19% | 289 | 150 | 92% | 203 |
| Net inflows (Rs bn) | 36 | 13 | 178% | 26 | 23% | 61 | 25 | 141% | 62 |
| Total Revenues | 1,466 | 748 | 96% | 1,347 | 9% | 2,814 | 1,332 | 111% | 3,413 |
| EBITDA | 359 | 140 | 157% | 347.789954 | 3% | 707 | 271 | 161% | 765 |
| PBT | 358 | 138 | 159% | 346.681055 | 3% | 705 | 268 | 162% | 759 |
| PAT | 233 | 92 | 154% | 231.825026 | 0% | 465 | 176 | 164% | 498 |

**MOVI or internal benchmark shows that benchmark values are difficult to find in the current market. What are we recommending potential sort of investors across mutual fund and PMS schemes. Are we recommending staggered investment or are we recommending part investment?**

We are still not resorting to any cash balance. We are investing 100% and we are suggesting the client that with a 10% downside outlook, immediately in near term you can have 10% downside, but we still think that on a 5-year basis doubling is possible, but the 10% downside possibility is one should take it very seriously, but client's mood is what it is right now. They basically look the upside, not the downside. That is a part of the profession and we do not know how long this financial shift in the whole segment is going to happen. If it goes on for 1 or 2 years, maybe we can just further stretch.

**We recently put 1% load across mutual and is it to debtor kind of investor who wants switch-in, switch-out and stick to the quality guys or now given our size and our performance and increased traction from the direct customers being almost 30% of AUM, so because of that we have changed this. What was the rationale?**

The rationale is what you said first that we need customers, who are a little bit a more serious than slipping because with no load, you can be in and out for 5 months, 6 months. We saw some trend in our redemption profile. We track our redemptions very closely. We are seeing the increasing trend of short-term guys coming and going and that was only leading to redemption. So we said we have to deter this and so that the quality of customers you have is somewhat more stable.

**We have seen good traction from last year's AUM base of 44 billion reaching 61 billion and cross-sell opportunities given that that is the number of clients are still being targeted in the product. So as a house, how do we blend the role of a manufacturer and a distributor given huge potential itself and the size in our mutual fund business and typically, what are the yields now on upfront and trail basis?**

First thing is that we have got different businesses which were handled by independent people. So the distribution business actually happens through two businesses. One is the broking, which is the retail mass broking and second thing is wealth management and both the businesses actually have open architecture system where they not only sell the group products, but they can also sell all the other products. So that is being taken care of by the structure as well as the open architecture.

Second thing about yield, that it is actually product to product like structures or private equity products would have structures which have high yield per se mutual funds really is a kind of normal yield. It is like about a percent or so net. Our target is to actually bring it at weighted average yield is about a percent on AMC side and equally slightly higher on the distribution side.

**Typically in mutual fund distribution, how much of it would be front-ended because earlier everything was front-ended and now laws have changed where part of it is front-ended as a distributor and part of it is trail?**

As far as MOAMC is concerned, we are not doing any front loading. Everything is on trail. Even on the distribution side also, most of the kind of money we want are on trail basis rather than just a front-ended side.

**What is the target in terms of market share of net sales?**

We are not targeting market shares. We are targeting absolute levels. The numerator is targeted, denominator is anybody's call. So we are pretty happy with about 1000 crore net sales per month. In fact the target for last year was little lower, actually we have achieved the full year target in 6 months only. So in this business, you can make your business plan, but what happens is what happens. Currently, our first criteria is the yield management rather than the AUM management and even before that is the performance management. But performance is internal in the sense facing the client, but as far as sales market is concerned, first is the yield, second is the AUM and now we have comfortable AUM of 30,000 crores plus. So financially, we are above breakeven. So now we want to focus bit on the yield management

**We have seen the direct sales contribution has risen from 13% to 30% now which is very encouraging. So ideally, where would we want to see this number of direct sales in our AUM better?**

We think 50% is the kind of dream kind of situation. And it is impacted by the sales marketing intensity, we have increased from start of this year. Particularly, you might have seen the “Think Equity Think Motilal Oswal” campaign in last 3-4 months. So that has a direct impact. Secondly, we have some success in the institutional side also in India because now the funds are more than 3 years old. So, now we can do marketing with the institutions and pension funds and all.

**If we encourage more of direct sales, it can cannibalize our distribution trail commission business right – wealth management, Distribution?**

No, there is no channel conflict, both are completely independent. We are seeing to it and there is no channel conflict and hence it is incremental in character, not cannibalizing each other.

It is definitely not and in any case, lot of things are happening at SEBI's end and on this distribution and all, but we are trying to see that there is no channel conflict and the client has to decide what he wants to do. it is a desirable trend which is happening in the system and we are trying to see that nobody in the process is hurt, nobody's pie is taken by anybody else.

**Is there any scope or opportunity for us to grab any business in terms of managing pension fund money?**

These are all very low yield and more debt oriented and things like that. So basically low yield business 1 paisa, 2 paisa, 5 paisa, we are not looking into that.

## Private Equity

**KEY FINANCIALS: PRIVATE EQUITY* (Rs Mn)**

| Particulars | Q2 FY18 | Q2 FY17 | CHG. YoY | Q1 FY18 | CHG. QoQ | H1 FY18 | H1 FY17 | CHG. YoY | FY17 |
|---|---|---|---|---|---|---|---|---|---|
| Total Revenues | 879 | 700 | 26% | 109 | 709% | 988 | 941 | 5% | 1,193 |
| EBITDA | 547 | 429 | 28% | 47 | 1075% | 594 | 561 | 6% | 649 |
| PBT | 543 | 427 | 27% | 41 | 1219% | 584 | 559 | 4% | 637 |
| PAT | 422 | 329 | 28% | 29 | 1363% | 451 | 450 | 0% | 502 |

## Wealth Management

**KEY FINANCIALS: PRIVATE WEALTH MANAGEMENT (Rs Mn)**

| Particulars | Q2 FY18 | Q2 FY17 | CHG. YoY | Q1 FY18 | CHG. QoQ | H1 FY18 | H1 FY17 | CHG. YoY | FY17 |
|---|---|---|---|---|---|---|---|---|---|
| AUM (Rs bn) | 129 | 86 | 51% | 113 | 14% | 129 | 86 | 51% | 101 |
| Net inflows (Rs bn) | 9 | 5 | 91% | 4 | 150% | 13 | 10 | 30% | 18 |
| Total Revenues | 267 | 174 | 53% | 179 | 49% | 446 | 328 | 36% | 720 |
| EBITDA | 111 | 52 | 112% | 59 | 87% | 170 | 88 | 93% | 223 |
| PBT | 109 | 46 | 137% | 57 | 91% | 165 | 74 | 124% | 205 |
| PAT | 78 | 31 | 151% | 40 | 95% | 119 | 50 | 137% | 132 |

## 3. Housing Finance Business

### Aspire Home Finance

**KEY FINANCIALS: ASPIRE HOME FINANCE (Rs Mn)**

| Particulars | Q2 FY18 | Q2 FY17 | CHG. YoY | Q1 FY18 | CHG. QoQ | H1 FY18 | H1 FY17 | CHG. YoY | FY17 |
|---|---|---|---|---|---|---|---|---|---|
| Loan Book (Bn) | 48 | 31 | 57% | 43 | 12% | 48 | 31 | 57% | 41 |
| Disbursements (Bn) | 6 | 7 | -5% | 3 | 92% | 10 | 11 | -16% | 24 |
| Gross NPL% | 2.8% | 0.3% | | 1.6% | | 2.8% | 0.3% | | 0.6% |
| Net Interest Income | 563 | 322 | 75% | 425 | 32% | 989 | 539 | 83% | 1,259 |
| Other Income | 224 | 279 | -20% | 155 | 45% | 379 | 455 | -17% | 951 |
| Total Income | 788 | 601 | 31% | 580 | 36% | 1,368 | 994 | 38% | 2,209 |
| Operating Profit | 468 | 375 | 25% | 284 | 65% | 752 | 600 | 25% | 1,379 |
| PBT | 345 | 345 | 0% | 213 | 62% | 558 | 552 | 1% | 1,257 |
| PAT | 223 | 227 | -2% | 141 | 58% | 365 | 361 | 1% | 821 |

**What will be our marginal cost of borrowing rate?**

Our 2Q cost of borrowing is 9.8%, but as we stated, we did not resort to any CPs in the first half which will be resorting to in the second half and so the incremental cost of borrowing in the second half should be lower than 9.8% because the cost of CPs will be well below 9.8%.

**In last 6 months, NPA numbers have gone up despite our loan book growth growing 50% plus. So how much will be your portfolio at risk default number? Can you give more insight about this increasing in the NPA because if I do on a two-year lag number basis, the NPA number looks 6% plus.**

We have reported our gross NPAs at 2.8%. As far as the other data points are concerned, investor relations team has made a note of it and will come back to you. Basically, we have seen very strong growth in our loan book in the last 2 years and as we have mentioned here, in the last 12 months, the three external shocks - demonetization, RERA and GST have had a direct impact both on the customers as well as the builders in the affordable housing space, particularly those who operate in the gram panchayat area rather than the municipal areas. Also, we relied on our sales and credit team for collection in the first 2-2.5 years. We have now put a dedicated collection engine and a legal engine as we have stated in place and we will see how this goes and the objective is obviously to bring this number down, but we will report to you as things progress over the coming quarters.

**How would RERA impact your NPA numbers or the borrower's ability to pay to you? Also, are RERA impact is in particular state or across all the regions where you operate?**

This is starker in the Mumbai region comprising of Kalyan, Panvel, Virar, more or less in Maharashtra, more accentuated in the Mumbai region.

**What will be the NPA split between your salary people and your non-salaried which is your salaried employee?**

We are not seeing any difference in the trend. Please bear in mind that a lot of these salaried employees are also cash salaried.

**During this quarter or last few quarters, how has been the repayment rate in our portfolio?**

Bounce rates are double digit in this business and so that is the number that we have shared with you in the past conference calls.

**Any particular geography where you see the major pain in this quarter?**

No, this is endemic to the space that we operate. There are obviously specific branches or where the NPLs are higher than your overall average. We have 120 of those branches. Of which, nearly 90 or about 85 to 90 are in the existing states. The range is always from 0 NPLs in some branch to higher than average in others. So there are pockets where the stress is more, but it may not necessarily be to do with that region as a whole. It could be to do with the underwriting in that particular branch also.

**When the PSU banks get lot of money and they entered to the housing finance market and they come out with a very aggressive pricing also. Now post that this recapitalization of banks, there is a concern that the market that vanilla product like housing finance will be the first product to disturb in terms of pricing. How do you see in our market?**

So the last 10 years, trend of home finance companies versus bank's share in the home finance product is quite clearly in favor of home finance companies. Within that, home finance companies' pie, the affordable housing piece is growing at nearly 1.5-2 times the Form 16 customers or the overall larger home finance companies growth rates. We think that even if banks were to enter this space, they would most likely operate in this space operated by the large HFCs and not really engage in sub one million rupee ticket size affordable home loan. We see lower chances of that happening.

**The decision to not have independent collection in legal team in place. Was it like thought through in the sense had you seen this in some other company and that is why you adopted it because otherwise it seems like a serious lapse in terms of structuring of the organization?**

Yeah, so basically the soft bucket collections are usually the responsibility anyways of the sales and the credit in all organizations that is not uncommon. And usually in the first couple of years of existence that is how most of home finance companies are structured, add to that the management team of Aspire also had a very strong view that brings better alignment from the point of view of the connect of the sales guys and the credit guys who have worked on their customer. So we think that assumption would have held correct if there were no meaningful external shocks. Some of them were unanticipated and we think maybe instead of year three and if we have done this in year 2, things would have been better off, but anyways in the year one or year two before the portfolio season and you have most of your loans at best in the soft bucket in the overdue 1 and 2 months. Usually that is anyways the responsibility of the sales and credit. So in hindsight, definitely you are right that it is a lapse and should have been an earlier. So we do not disagree with you on that at all.

**What kind of this recovery mechanism you have, it is like independent in-house or is it like independent outsource?**

It is independent in-house. So as usual, the first one and two month bucket is supplemented by external call centers supported by the sales and credit and then as far as the 3, 4, 5, 6 month onwards is concerned, it is all taken care of by captive in-house collection team. We are 92 strong collection team now as of 30th September and is also supported by the legal team which is engaged in all the necessary filings including section 138, section 13(2), section 13(4), section 14 and so on, arbitration, Lok Adalat. So whatever legal recourse or means are available under the law are being taken besides the early call center activation, RM credit involvement in the soft buckets and the 92 strong collection team from the 3-month onward bucket.

**How is this industry stacked up now because as RERA, GST and demonetization impacting and we have also slowed down slightly on the disbursement side of it, to be on the cautious side, but in last 3-4 years we have seen many companies coming into this space. So is there a chance of this industry where the capacities have come up and demand as of now for the last 8-9 months have kind of, not the most desired kind of demand because we would like to lend very prudently. So how is this industry shaping up basically?**

We would suggest and request that do not read too much into the Aspire result as a trend in the industry or anything like that. We are young company, new company, as a promoter we are new. So there is lot of learning. There is a good thing that this demonetization all this thing happened to open our eyes that where are the gaps in our processes and all that are all being put in place and we are very sure that the opportunity is very large and really huge opportunity. We do not think it is a capacity issue or business opportunity issue. It is about how well you execute. So that execution excellence which was wherever the gaps were, we think it is our job to put in place and there is no reflection on the industry.

**How much time would this impact remain as far as RERA and GST is concerned for the Housing as a sector and then on the Housing Finance as a sector?**

Our sense is that nobody knows what is going to happen in next 12 months, but last 12 months what we have gone through, we do not think that is going to repeat and hence it is a continuous work in progress, we are becoming better every day, and new process are coming in. We think things are stable now and by Q3-Q4, we will get to see that things are falling in place and our process is superior, so our execution must improve.

## 4. Fund-based Business

**KEY FINANCIALS: MOFSL Standalone (Rs Mn)**

| Particulars | Q2 FY18 | Q2 FY17 | CHG. YoY | Q1 FY18 | CHG. QoQ | H1 FY18 | H1 FY17 | CHG. YoY | FY17 |
|---|---|---|---|---|---|---|---|---|---|
| Total Revenues | 957 | 788 | 21% | 226 | 324% | 1,183 | 1,367 | -13% | 1,763 |
| EBITDA | 906 | 743 | 22% | 176 | 415% | 1,082 | 1,265 | -15% | 1,569 |
| PBT | 798 | 549 | 45% | 71 | 1032% | 869 | 752 | 15% | 857 |
| PAT | 625 | 569 | 10% | 49 | 1167% | 674 | 748 | -10% | 863 |

## INVESTOR UPDATE

# Motilal Oswal Financial Services reports Q2FY18 Consolidated Revenues of Rs 7.14 billion, +35% YoY; and PAT of Rs 1.44 billion, +42% YoY

**Mumbai, November 04, 2017:** Motilal Oswal Financial Services Ltd. announced its results for the quarter ended September 30, 2017 post approval by the Board of Directors at a meeting held in Mumbai on November 04, 2017.

**Performance Highlights**

| Rs Million | Q2FY18 | Q2FY17 | YoY Chg | Q1FY18 | QoQ Chg |
|---|---|---|---|---|---|
| **Revenues** | 7,144 | 5,285 | ↑35% | 5,761 | ↑24% |
| **PBT** | 2,314 | 1,486 | ↑56% | 1,386 | ↑66% |
| **PAT** | 1,437 | 1,016 | ↑42% | 1,016 | ↑41% |
| **EPS (FV-1)** | 10 | 7 | | 7 | |

**Performance for the quarter ended September 30, 2017**

- Consolidated revenues were Rs 7.1 billion in Q2FY18, +35% YoY.
- Strong growth in Q2FY18 across businesses. Asset & Wealth Management business top-line was up 62% YoY, Housing finance was +22% YoY, and Capital Market businesses +20% YoY. The revenue mix is seeing healthy diversification, as 61% of the revenue came from linear sources like Asset & Wealth Management and Housing Finance. While the share of Capital Markets reduced in the mix (34% in Q2FY18), it continues to grow strongly in absolute terms. Both, Asset Management and Housing finance businesses, saw strong growth in assets, and improved in profitability despite significant investments in manpower, distribution network and marketing.
- PBT was up by 56% YoY at Rs 2.3 billion. Consolidated PAT was Rs 1.4 billion in Q2FY18, +42% YoY. This incremental PAT growth was contributed by Asset & wealth management business (+52% YoY) and Capital Market business (+38% YoY).
- Significant investments have been made into manpower in Broking (+44% YoY) and Housing Finance (+68% YoY). Ad expenses are +51% YoY in Asset Management business. These up-fronted investments will translate into operating leverage in the coming year. Some of this was visible, with PAT Margin of 20% in Q2FY18. However, the full effect of operating leverage is yet to unfold in our businesses.
- As of September 2017, Net worth was Rs 20 billion, Gross borrowing was Rs 55 billion and Net borrowing was Rs 51 billion (including Aspire). Excluding Aspire, Gross and Net borrowings were Rs 15 billion and Rs 12 billion respectively. Balance sheet has strong liquidity, with ~Rs 13 billion as of September 2017 in near-liquid investments to fund any future investment needs of operating businesses.
- In line with our strategy to deliver sustainable 20%+ RoE in the long term, RoE for Q2FY18 was 29% on reported PAT. However, this does not include unrealised gains in our quoted equity investments (Rs 5.8 billion, as of September 2017). Including this, the RoE in Q2FY18 would have been ~32%.

**Speaking on the performance of the company, Mr. Motilal Oswal, CMD said**

*"Our strategy to diversify our business model towards linear sources of earnings like Asset Management and Housing Finance continues to show results, with over half of the revenue pie now coming from these new businesses. Each of these businesses offer significant headroom for growth and operating leverage as they scale up. Even our traditional businesses also saw decisive uptick during the quarter by registering record revenues. With this strategy, we have achieved highest ever quarterly revenue and profit during Q2FY18 and H1FY18. Our brand is now being recognized in each of our businesses".*

**Performance of Business Segments for the quarter ended September 30, 2017**

- **Capital markets Businesses (Broking & Investment banking)**
  - **Capital Market** revenues in Q2FY18 were Rs 2.4 billion, +20% YoY. Market ADTO grew 65% YoY in Q2FY18, with F&O +68% YoY and cash +21% YoY. Our market share in high-yield cash segment was improved on sequential basis and overall market share improved to 2% in Q2FY18. Blended yield maintained at 2.9% in H1FY18. Some of the operating leverage from the investment in manpower (+44% YoY), brand & technology is visible, as PAT margin is at 17% in Q2FY18. However, the full benefit of operating leverage is yet to unfold.
  - **In retail broking & distribution**, our strategy to bring in linearity through the trail-based distribution business is showing results. Distribution Net Sales were Rs 8.2 billion in Q2FY18, +142% YoY, and AUM was Rs 61 billion, +130% YoY. Distribution income at 15.9% of retail broking net revenues. With only ~9% of our client base and ~18% of the distribution network tapped as of now, we expect a meaningful increase in AUM and fee income as cross-selling increases. Our efforts to improve sales productivity is bearing fruit, with over 60% of leads generated online. Online business continues to grow, reaching 42% of retail volumes in Q2FY18.
  - **In institutional broking,** blocks continued to gain solid traction within our volumes. Our empanelled trend remains strong with 15 new client additions during the quarter. Focus has been on making the most of the market tailwind while building sustained areas of competitive advantage.
  - **Investment banking** continues to have a strong pipeline. IB fee were Rs 465 million in Q2FY18, +59% YoY. Our IB was among the top 10 investment banks in primary market equity deal ranking in H1CY17. It has completed 7 ECM transactions in H1FY18.
  - Capital markets businesses contributed ~34% of revenues in Q2FY18. The contribution of capital markets in the PAT mix was ~29% in Q2FY18.

- **Asset Management businesses are nearing critical mass**
  - Asset Management business across MF, PMS & AIF reached the mark of Rs 290 billion AUM this year, comprising of Rs 143 billion MF AUM and Rs 134 billion PMS AUM. Our AMC now ranks among the Top-10 players by total equity assets with leadership position in PMS business. Net Sales were Rs 61 billion in H1FY18, +141% YoY and compares with Rs 62 billion in all of FY17. AUM was Rs 290 billion, +92% YoY. Net yield was maintained at ~0.9% in Q2FY18. Revenues were Rs 1.46 billion in Q2FY18, +96% YoY and PAT is Rs 233 million, +154% YoY despite significant investments in brand building. The asset management business offers significant headroom for growth and operating leverage.
  - Our QGLP philosophy continued to deliver on investment performance; our F-35 scheme has delivered absolute returns of 31% and alpha over benchmark of 16%, since inception. Our 3 flagship mutual funds schemes completed their 3-year performance track record, leading to increased participation from distributors.
  - With equity mutual funds focusing on retail outreach, PMS and AIF serve HNIs, family offices and institutions and are able to differentiate with concentrated strategies affording scope for higher alpha.
  - As of Sep 2017, ~15% of non-mutual fund AUM is performance-fee linked, and our target is to increase this further.
  - Our market share in Equity MF Net Sales has scaled up in Q2FY18 to ~4.3% compared to 3.6% in Q2FY17. Due to our recent vintage, our market share in Equity MF avg AUM is ~1.8%.
  - Ad & marketing spends were Rs 85 mn in Q2FY18, +51% YoY and 85% QoQ, forming 14% of net revenues.

- Our ongoing ad campaign "Think Equity Think Motilal Oswal" is reiterating our positioning as equity specialist. These branding exercise and strong performance of our products coupled with higher equity inflows in market are helping us to garner higher market share.
- Significant investments in manpower and advertising have been up-fronted, which could result in a meaningful operating leverage in the future. With increase in financial savings to total savings, the domestic market should continue to benefit from this shift towards financial assets. In offshore, which is 1.7x of institutionally managed equity assets in India, we are seeing initial interest in our offshore products.

- **In private equity,** we manage an AUM of Rs 42 billion across 3 growth capital PE funds and 3 real estate funds. The PE business has demonstrated robust profitability and scalability. The 1st growth fund (IBEF 1) has delivered an XIRR of 29%, and alpha of 10% and is expected to return ~5x MoC (Multiple of Cost). Till date, 2.5x MoC has been return for INR investors and 2.2x for USD investors. Exits across our 6 funds at strong IRRs bring linearity to income stream. Strong performance and positioning is also aiding new fund raise. Fund III (IBEF III) launched during the quarter and received phenomenal response by garnering 10 billion and expected to close FY18 with corpus of Rs 20 billion.
- **In Wealth Management,** business AUM grew 51% YoY to Rs 129 billion. Highest-ever net sales at Rs 9.1 billion, +91% YoY. We have achieved highest-ever EBITDA margin of 41% for the quarter resulting out of improved RM productivity in line with vintage. Our capacity to hire additional RMs will increase as existing RMs vintage increases which will which will help sustaining growth and driving further operating leverage.
- Asset and Wealth Management revenue were Rs 2.5 billion in Q2FY18, +61% YoY. This now contributes to ~36% of consolidated revenues in Q2FY18 vs 30% back in Q2FY17. Contribution of Asset & Wealth Management in the Profit mix was ~50% in Q2FY18 vs 46% in Q2FY17.

- **Housing finance has shown traction in loan book, while maintaining risk and operational parameters**
- Housing finance loan book grew by 57% YoY at Rs 48 billion.
- NII grew 75% YoY to Rs 564 million, as interest expenses declined, driven by lower borrowings and lower cost of funds. PAT remained stable YoY at Rs 223 million.
- Strong ramp up in last year has driven 70% YoY growth in manpower and 62% growth in branches. However, YTD growth in manpower is 19% with no additions to branches.
- We have maintained steady operating metrics. The average ticket-size was Rs 0.90 million, LTV of ~58% and FOIR of ~46% as of September 2017.
- Disbursements in Q2FY18 were Rs 6.3 billion versus Rs 3.3 billion in Q1FY18 and Rs 6.7 billion in Q2FY17. Calibration in the pace of disbursements in H1FY18 was partly led by external factors in the economy, causing postponement of customer decisions. Investments have been made in building a collection and legal organisation while calibrating growth. This will create a strong foundation for sustainable growth.
- GNPA increased from 1.6% in Q1FY18 to 2.8% in Q2FY18 on account of seasoning of the book coupled with external shocks such as demonetization, RERA and GST. Also, in the first three years, absence of independent collection and legal organization, resulted in higher slippages. The collection and legal engine is now in place.
- Average yield held firm at ~13.4% on a YoY basis despite competition.
- In liabilities, ~53% borrowings were from NCDs and ~47% from bank loans. As of September 2017, 26 Banks/NBFC had extended lines, apart from 24 institutions to whom NCDs were allotted.

- Our credit ratings are CRISIL A+ Stable and ICRA AA-. We have kept gearing conservative, with the Debt/Equity ratio at 5.1x.
- Strong traction in margin at 4.5% in Q2FY18 on account of lower incremental borrowings and sequentially lower cost of funds. Equity infusion in Q1FY18 also aided margin expansion.
- Average cost of borrowings declined from 10% in Q2FY17 to ~9.8% in Q2FY18, despite negligible CP contribution in funding mix. Incremental borrowings from CP will bring down cost of borrowings in H2FY18.
- ROA for Q2FY18 was 1.7%, while RoE was 11.6%.
- Cumulative capital infusion from sponsor is Rs 6 billion and net worth is Rs 7.7 billion, as of September 2017.
- We have been investing in technology to strengthen our database, analytics and risk framework. We are also investing in digital initiatives to reduce operating costs and turnaround time, and to improve customer experience. Our digital initiatives include new apps for sales, credit, collection, clients and vendors.
- Aspire has been awarded the second prize for "Best Performing PLI (prime lending institution) under PMAY by MHUPA (Ministry of Housing and Urban Poverty Alleviation)".

- **Fund based business** includes sponsor commitments to our AMC & PE funds, equity investments and NBFC LAS book.
  - Fund based business income grew +324% to Rs 957 million in Q2FY18, largely driven by dividend of Rs 458 million from PE on account of carry income of Rs 539 million.
  - Unrealized gain on quoted equity investments (equity MF/Shares) as of September 2017 is Rs 5.8 billion (equity MF: Rs 4.1 billion against Rs 6.7 billion investment at cost; AU Small Finance Bank: Rs 1.7 billion). This is not reflected in the reported PAT; had this been included, RoE would have been ~32% against the reported 29%.
  - Reported RoE of 4% in fund based business; however, post-tax cumulative XIRR of ~29% (since inception) on equity investments, validating the long-term performance track record of our QGLP investment philosophy.
  - These investments have helped "seed" our new businesses, which are scalable, high-RoE opportunities. They also serve as highly liquid "resources" available for future investments in business, if required.
  - Our investments in Motilal Oswal's alternative investment funds stood at Rs 2.9 billion.
  - NBFC LAS lending book was Rs 2.24 billion as of September 2017, which is run as a spread business.

- In line with the goal to achieve a sustainable 20%+ RoE, consolidated RoE for the Group for 21FY18 was 29% (without including unrealized gains on quoted equity investments of Rs 5.8 billion). Within this, Asset and Wealth Management RoE was 308%, Capital Markets RoE was 86% and Housing Finance RoE was 12%.

**About Motilal Oswal Financial Services Limited**

Motilal Oswal Financial Services Ltd. is a financial services company. Its offerings include capital markets businesses (Retail broking, Institutional broking & Investment banking), Asset & Wealth Management (Asset Management, Private Equity & Wealth Management), Housing Finance & Equity based treasury investments. Motilal Oswal Securities won the 'Best Performing National Financial Advisor Equity Broker' award at the CNBC TV18 Financial Advisor Awards for the 6th time. It was ranked the Best in Events/Conferences, ranked amongst Top-2 for Overall Sales Services & Best Roadshows/Company Visits & amongst the Top-3 in Best Local Brokerage, Best Execution & Sales Trading Visits at the Asia Money Awards 2015. Motilal Oswal Private Equity won the 'Best Growth Capital Investor-2012' award at the Awards for PE Excellence 2013. Motilal Oswal Private Wealth Management won at the UTI-MF CNBC Financial Advisor Award in

HNI Wealth Management category for 2015. Aspire Housing Finance was awarded 'India's Most Admired & Valuable Housing Finance Company' at India Leadership Conclave 2015.

**For further details contact:**


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| Mrs. Rohini Kute<br>(Head of Corporate Communication)<br>Motilal Oswal Financial Services<br>Ph- +91-22-30102340,<br>Mob- +91-9820196838 | Mr. Shalibhadra Shah<br>(Chief Financial Officer)<br>Motilal Oswal Financial Services<br>Ph- +91-22-39825500<br>Mob- +91-9819060032 | Mr. Alpesh Nakrani<br>Paradigm Shift Public Relations<br>Ph- +91-22 22813797<br>Mob- +91-9892343828 / +91-9869121167 |