Earnings Update – Q3 FY14

Jan 21, 2014

Motilal Oswal Financial Services Limited

BSE: 532892 ● NSE: MOTILALOFS ● Bloomberg:MOFS:IN ● Reuters: MOFS.BO

www.motilaloswal.com

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Motilal Oswal Financial Services

Q3 FY14 performance

Consolidated financials

Business snapshots

About us

Thematic series

Industry facts

Q3 FY14 performance | Consolidated financials | Business snapshots | About us | Thematic series | Industry facts

Highlights – Q3 FY14

Consolidated Financials	• Revenues in Q3 FY14 were ₹1.2 billion (up 1% QoQ and up 2% YoY) • Adjusted PAT in Q3 FY14 was ₹162 million (down 14% QoQ and down 14% YoY) • Reported PAT was ₹35 million (down 37% QoQ and down 88% YoY) • EBITDA and Adjusted PAT margins for Q3 FY14 were 26% (31% in Q2 FY14) and 14% (16% in Q2 FY14) respectively • The balance sheet had net worth of ₹11.8 billion and net cash of ₹1.5 billion, as of Dec 2013 • Pursuant to the commencement of the buy-back programme of the company's shares at a price not exceeding ₹90 per share of upto a maximum of 7.5 million shares, the company has bought back 6.5 million shares as of Dec 2013
Volumes and Market Share	• Total ADTO in secondary equities was ₹32.0 billion in Q3 FY14 (₹31.7 billion in Q2 FY14 and ₹25.5 billion in Q3 FY13) • Equity market share was 1.7% in Q3 FY14 (1.4% in Q2 FY14 and 1.5% in Q3 FY13)
Distribution Reach	• Retail distribution stood at 1,546 business locations across 519 cities, as of Dec 2013 • Total client base increased to 792,858 which includes 695,663 retail broking and distribution clients
Assets Managed	• Total assets under management/advice across mutual funds, PMS and private equity businesses was ₹35.2 billion. Within this, our mutual funds AUM was ₹4.8 billion, PE AUA was ₹17.0 billion, while PMS AUM was ₹13.4 billion • Private Wealth management business managed assets of ₹23.2 billion • Depository assets were ₹129.0 billion
Business Updates	• Motilal Oswal Investment Banking won 'M&A Boutique Firm of the Year' and 'Best Mid-Market Deal of the Year' awards at the M&A Atlas Awards in Mumbai • Motilal Oswal Private Equity received final approval from SEBI for its 2nd real estate fund, India Real Estate Fund-II. It is currently in fund raising mode • MOFSL conducted its 18th Annual Wealth Creation Study in December, 2013

Q3 FY14 performance

Consolidated financials

Business snapshots

About us

Thematic series

Industry facts

Consolidated financials

Particulars	Q3 FY14	Q2 FY14	Change	Q3 FY14	Q3 FY13	Change	9M FY14	9M FY13	Change	FY13
₹million	Dec 31, 2013	Sep 30, 2013	(%) Q-o-Q	Dec 31, 2013	Dec 31, 2012	(%) Y-o-Y	Dec 31, 2013	Dec 31, 2012	(%) Y-o-Y	Mar 31, 2013
Total Revenues	1,175	1,160	1%	1,175	1,150	2%	3,443	3,388	2%	4,729
EBIDTA	309	358	-14%	309	378	-18%	1,023	1,144	-11%	1,744
PBT (before E & EOI)	239	290	-18%	239	300	-20%	817	930	-12%	1,437
Adjusted PAT	162	188	-14%	162	189	-14%	535	621	-14%	969
Reported PAT	35	56	-37%	35	292	-88%	276	724	-62%	1,091
EPS - Basic	0.3	0.5		0.3	2.0		2.1	5.0		7.6
EPS - Diluted	0.3	0.5		0.3	2.0		2.1	5.0		7.6
No.of shares outstanding (million) - FV Rs 1/share	139	139		139	145		139	145		145

E & EOI = Exceptional items & Extraordinary items

- Motilal Oswal Group has exposure to National Spot Exchange Limited (NSEL). However, NSEL has not been able to adhere to its payment obligations. The Group has perused legal action against NSEL. Pending final outcome which is uncertain, the company has provided for an amount of ₹126.8 million (post tax) in respect of these positions for the quarter ending Dec 2013 (cumulative ₹258.4 million post tax till date), which is disclosed under the head “Exceptional Items”

Revenue composition

Particulars	Q3 FY14	Q2 FY14	Change	Q3 FY14	Q3 FY13	Change	9M FY14	9M FY13	Change	FY13
₹million	Dec 31, 2013	Sep 30, 2013	(%) Q-o-Q	Dec 31, 2013	Dec 31, 2012	(%) Y-o-Y	Dec 31, 2013	Dec 31, 2012	(%) Y-o-Y	Mar 31, 2013
Brokerage & operating income	738	732	1%	738	779	-5%	2,149	2,220	-3%	2,964
Investment banking fees	5	35	-84%	5	20	-73%	48	70	-31%	78
Fund based income	199	179	11%	199	200	-1%	645	620	4%	1,005
Asset management fees	193	206	-6%	193	139	39%	524	418	25%	599
Other income	40	8	370%	40	12	228%	76	60	27%	82
Total Revenues	1,175	1,160	1%	1,175	1,150	2%	3,443	3,388	2%	4,729

- Broking and related revenues were ₹738 million in Q3 FY14, marginally up by 1% on a QoQ basis and down 5% on a YoY basis. This segment contributed 63% of the total group revenues
- Investment banking fees at ₹5 million was down 73% YoY. Transaction closures remain impacted as multiple macro concerns continue to affect the investment mood in the economy
- Fund based income was ₹199 million, up 11% from Q2 FY14 and marginally down 1% from Q3 FY13. The loan book was ₹4.3 billion, as of Dec 2013
- Asset Management fee were ₹193 million for Q3 FY14, down 6% QoQ and up 39% YoY. This includes fees booked on final closing of the offshore leg of the new private equity fund, IBEF II
- Other income was ₹40 million in Q3 FY14

Q3 FY14 performance

Consolidated financials

Business snapshots

About us

Thematic series

Industry facts

Motilal Oswal Securities Ltd (MOSL)

Retail Broking & Distribution and Institutional Equities

Particulars ₹million	Q3 FY14 Dec 31, 2013	Q2 FY14 Sep 30, 2013	Change (%) Q-o-Q	Q3 FY14 Dec 31, 2013	Q3 FY13 Dec 31, 2012	Change (%) Y-o-Y	9M FY14 Dec 31, 2013	9M FY13 Dec 31, 2012	Change (%) Y-o-Y	FY13 Mar 31, 2013
Total Revenues	817	774	6%	817	842	-3%	2,366	2,486	-5%	3,369
EBIDTA	222	212	5%	222	242	-8%	668	790	-15%	1,076
PBT (before E & EOI)	177	169	5%	177	192	-8%	542	653	-17%	887
Adjusted PAT	123	122	0%	123	115	6%	369	430	-14%	588
Reported PAT	9	4	112%	9	218	-96%	138	533	-74%	821

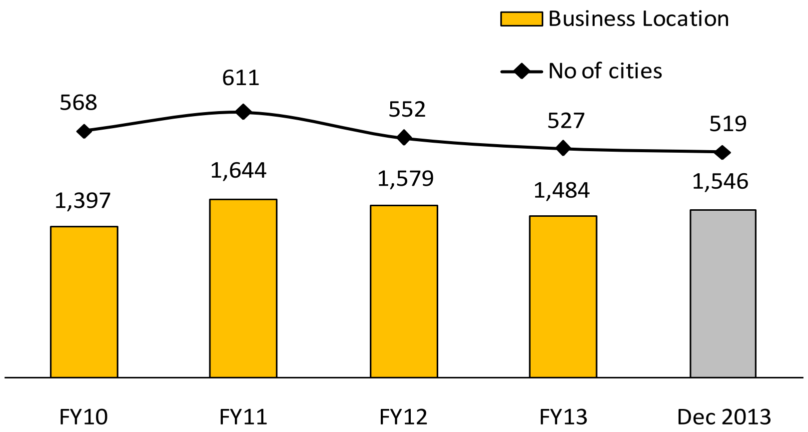
E & EOI = Exceptional items & Extraordinary items

- Revenues were ₹817 million for Q3 FY14, up 6% on a QoQ basis and down 3% as compared to Q3 FY13
- Adjusted PAT was ₹123 million for Q3 FY14, flat on a QoQ basis and up 6% YoY. Reported PAT was ₹9 million, up 112% QoQ and down 96% YoY. MOSL has exposure to NSEL. However, NSEL has not been able to adhere to its payment obligations. MOSL has perused legal action against NSEL. Pending final outcome which is uncertain, the company has provided for an amount of ₹113.3 million (post tax) in respect of its proprietary position for the quarter ending Dec 2013 (cumulative ₹231.1 million post tax till date), which is disclosed under the head "Exceptional Items"
- MOSL ADTO in secondary equities was ₹32.0 billion in Q3 FY14 (₹31.7 billion in Q2 FY14 and ₹25.5 billion in Q3 FY13)
- Equity market ADTO were ₹1.9 trillion in Q3 FY14, a 15% drop on a QoQ basis. This was largely led by an 18% QoQ drop in options specifically. Options now comprise 75% of market volumes, as compared to 78% in the previous quarter. Cash volumes were down by 4% QoQ to ₹130.9 billion, and its proportion within market volumes picked up from 6.2% to 7%. Our overall equity market share increased from 1.4% to 1.7% on a QoQ basis, led by gains in both the cash and F&O market shares. Our blended yield, at 3.7 bps, has held firm on a QoQ basis

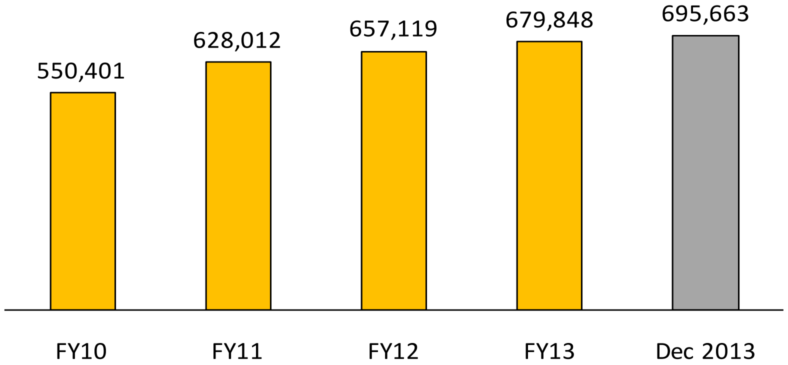
Broking and Distribution

- Offers customized investment services to its retail customers
- 'Customer first' philosophy executed through strategic focus on:
  - Creating a robust Pan-India distribution network
  - Customer segmentation based on individual needs
  - Offerings include equity, PMS, MFs, commodities, currency
  - Develop in-house technology for better customer experience
  - Intensify customer connect through seminars and feedback

Pan-India distribution footprint



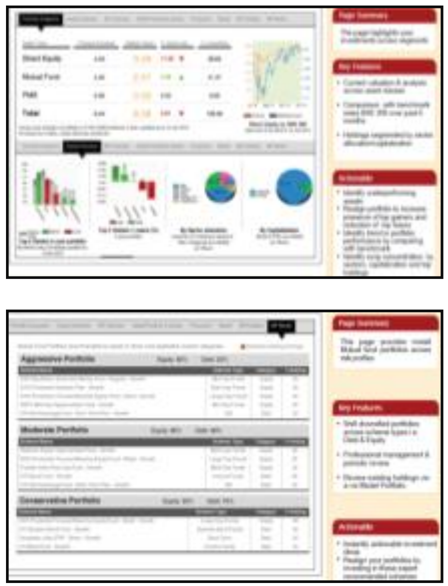
Retail broking and distribution clients



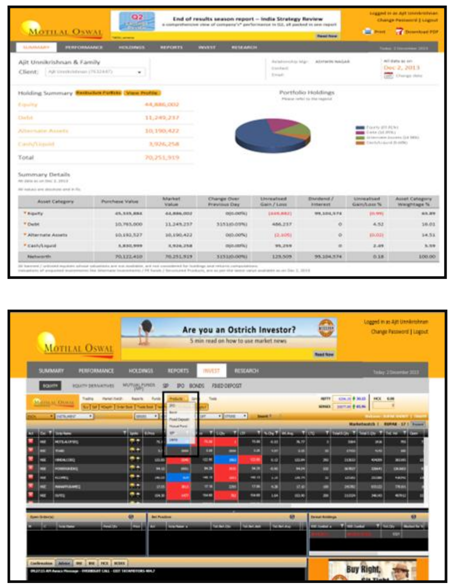
We are continuously innovating with our trading platforms to ensure a superior experience for our broking customers. During the quarter:-

- Added Spread Order Facility for NSE F&O & NSE Currency
- Added AMO (After Market Order) functionality in Lite Platform
- Positional Trade Guide Signal on Nifty stocks, it generates Long and Short signals when breakout occurs from normal volatility range. It may also generate sequence of buy & sell signals
- Radar, a news dashboard, now has a midcap valuation guide
- Portfolio Check, an algo-based portfolio restructuring tool, gives instant expert views on stocks to be held, added, sold
- Developed Client Portal for third-party distribution clients, wherein clients can track/review portfolio, and do investments

Portfolio Check



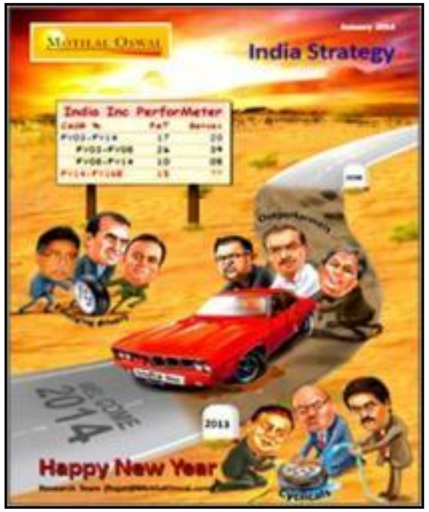
Client Portal

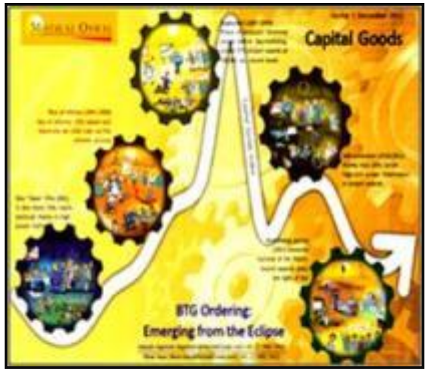


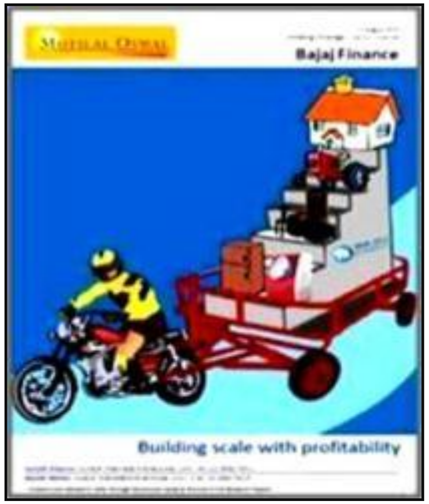
Institutional Equities – Quality Research

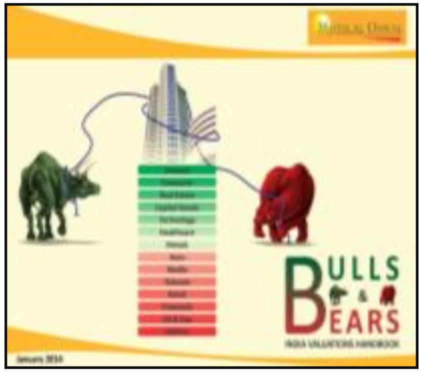
- Cash and derivatives broking to institutional clients, along with a strong research and corporate access group
- Client base of 543 institutions, as of Dec 2013
- Won the Best Market Analyst Award for the category Equity-Auto at Zee Business India's Best Market Analyst Awards 2013
- Conducted the 9th Annual Motilal Oswal Global Investor Conference in Mumbai in Sep 2013. Over 100 leading companies interacted with more than 600 investors from all over the world, translating into 3,000+ company-investor meetings

Recent Research Reports









Private Wealth Management

- Private wealth management business had a total AUM of ₹23.2 billion, as of Dec 2013
- Our new and improved advisory proposition 'Motilal Oswal Private Wealth Management (MOPWM)' with the motto 'Responsible Advisory' was launched in Q4FY13. The value proposition is based on comprehensive risk profiling leading to portfolio advice which can be objectively tracked for value addition. MOPWM also launched India's first Advisory Index and other indices which will help clients track the value addition by an advisor objectively - an Industry First
- Clients will have access to a multi asset class open architecture platform
- Present in Mumbai, Delhi, Kolkata, Bangalore, Hyderabad, Ahmedabad and Pune

Our Offerings: A comprehensive menu of Multi Asset Class Advisory Solutions

Professional Money Managers
- Mutual Funds
- PMS
- Alternative Invst. Funds

Trading
- Equity
- Fixed Income
- Commodity & Currency

Alternative Assets
- Private Equity
- Real Estate
- Structured Products

Credit Solutions
- IPO Financing, ESOP Funding
- LAS/LAP
- Institutional Credit Solutions

Wealth Transmission
- Estate Planning
- Trust services
- Wills

Specialized Services
- Investment Bnkg. Services
- Offshore Advisory & Solutions
- Hedging & Insurance Advisory

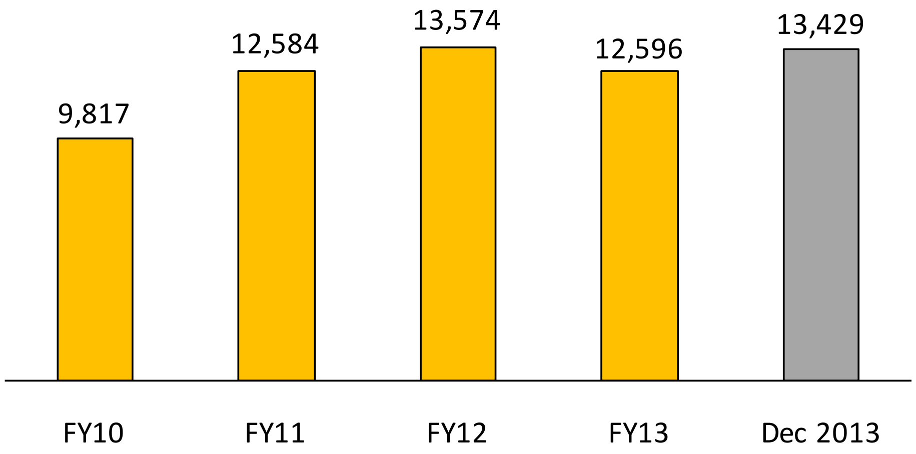
Ancillary Services
- Tax Advisory
- Legal Advisory

Asset management

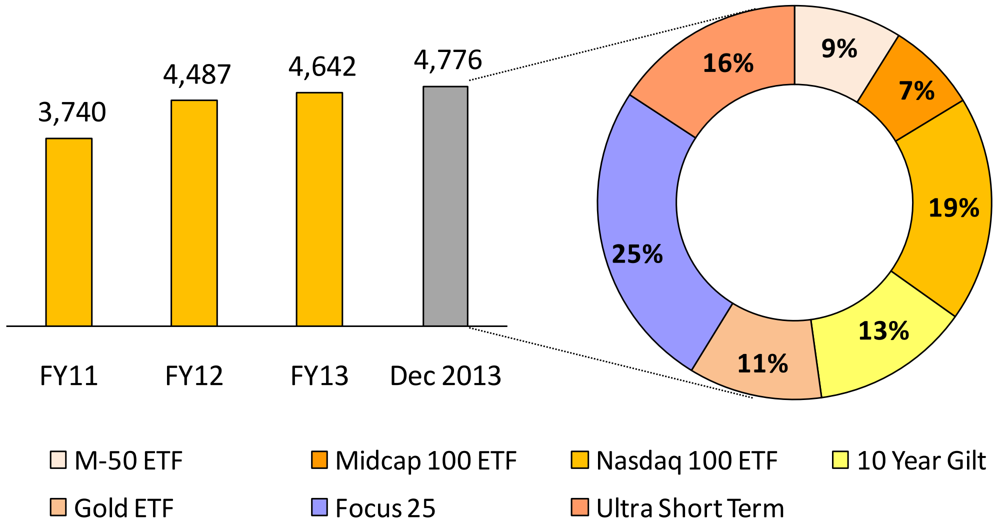
Particulars ₹million	Q3 FY14 Dec 31, 2013	Q2 FY14 Sep 30, 2013	Change (%) Q-o-Q	Q3 FY14 Dec 31, 2013	Q3 FY13 Dec 31, 2012	Change (%) Y-o-Y	9M FY14 Dec 31, 2013	9M FY13 Dec 31, 2012	Change (%) Y-o-Y	FY13 Mar 31, 2013
Total Revenues	66	69	-5%	66	79	-17%	205	260	-21%	348
EBIDTA	(8)	(8)	nm	(8)	13	nm	(29)	47	nm	58
PBT (before E & EOI)	(9)	(9)	nm	(9)	11	nm	(32)	43	nm	53
Reported PAT	(9)	(9)	nm	(9)	11	nm	(31)	43	nm	53

E & EOI = Exceptional items & Extraordinary items

PMS AUM (₹ million)



Mutual Funds AUM (₹ million)



- As of Dec 2013, PMS AUM was ₹13.4 billion and mutual funds AUM across the 7 funds was ₹4.8 billion

Investment banking

Particulars	Q3 FY14	Q2 FY14	Change	Q3 FY14	Q3 FY13	Change	9M FY14	9M FY13	Change	FY13
₹million	**Dec 31, 2013**	**Sep 30, 2013**	**(%) Q-o-Q**	**Dec 31, 2013**	**Dec 31, 2012**	**(%) Y-o-Y**	**Dec 31, 2013**	**Dec 31, 2012**	**(%) Y-o-Y**	**Mar 31, 2013**
Total Revenues	11	45	-75%	11	20	-42%	65	72	-9%	80
EBIDTA	(19)	16	nm	(19)	(9)	nm	(25)	(39)	nm	(60)
PBT (before E & EOI)	(23)	12	nm	(23)	(11)	nm	(36)	(44)	nm	(68)
Reported PAT	(15)	8	nm	(15)	(8)	nm	(24)	(32)	nm	(52)

E & EOI = Exceptional items & Extraordinary items

- The investment climate continues to be vitiated due to macro uncertainties and policy paralysis. As a result, transaction closures have been affected, though the deal pipeline remains healthy
- The company continues to focus on building its capabilities in identified sectors and product lines
- 25 employees in investment banking, as of Dec 2013
- Motilal Oswal Investment Banking won ‘M&A Boutique Firm of the Year’ and ‘Best Mid-Market Deal of the Year’ awards at the M&A Atlas Awards in Mumbai

Private equity

Particulars	Q3 FY14	Q2 FY14	Change	Q3 FY14	Q3 FY13	Change	9M FY14	9M FY13	Change	FY13
₹million	Dec 31, 2013	Sep 30, 2013	(%) Q-o-Q	Dec 31, 2013	Dec 31, 2012	(%) Y-o-Y	Dec 31, 2013	Dec 31, 2012	(%) Y-o-Y	Mar 31, 2013
Total Revenues	135	143	-6%	135	71	91%	338	184	83%	274
EBIDTA	70	83	-16%	70	29	140%	175	51	246%	82
PBT (before E & EOI)	69	82	-16%	69	28	146%	172	48	259%	78
Reported PAT	46	54	-15%	46	19	141%	114	33	250%	53

E & EOI = Exceptional items & Extraordinary items

- India Business Excellence Fund (IBEF) is a growth capital fund focused on the SME space with AUM of US$ 125 million, which has been fully committed across 13 companies. The fund has partially exited two holding companies till date via secondary sales at extremely healthy multiples. The fund has returned approximately 40% of capital to its investors so far
- India Realty Excellence Fund (IREF) is a domestic real estate fund with total AuA at ₹2 billion, which has been fully committed across 7 deals. Following full/partial exits from four projects till date, the fund has returned approximately 50% of capital to its investors so far
- The 2nd growth capital PE fund, India Business Excellence Fund-II, has received total commitments of approximately ₹9.5 billion from both domestic and offshore investors. This fund is currently evaluating several investment opportunities and has made two investments so far
- Our 2nd real estate fund, India Real Estate Fund-II has received final approval from SEBI and is currently in fund raising mode. This is a ₹3 billion domestic mezzanine real estate fund with a green shoe option of ₹2 billion

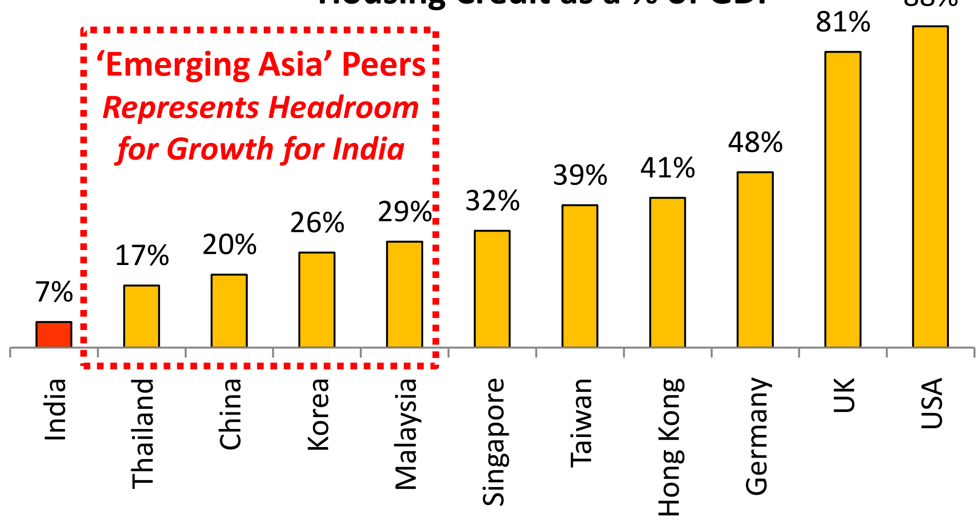
Aspire Home Finance Corporation Ltd.

During Q2FY14, we invested into building a new housing finance company – **Aspire Home Finance Corporation Limited (http://www.ahfcl.com).** This is being led by Anil Sachidanand, previously with DHFL as CEO. He brings with him 22 years of rich experience in the mortgage space. We are currently in the process of obtaining the necessary approvals for commencement of this business. It will be our endeavor to build a high quality institution with a strong value proposition which we believe can help us capture a sizable portion of this opportunity and add significant value for all stakeholders

Housing finance: A promising opportunity

- **Low Penetration**: India's mortgage/GDP ratio improved from 4.5% in FY04 to 7% in FY12. However, it is still low vs. peers
- **Potential in Tier II/III cities**: Mortgage growth has tilted towards tier-II/III cities in recent years
- **Young median age and its expected growth**: Translates into an increased working population and demand for housing
- **Changing social factors**: Increased urbanization and rise of nuclear families expected to boost the demand for dwelling

Housing Credit as a % of GDP



Other Positive developments

- Market share of HFCs vs. Banks has increased from 26% to 35% from FY05 to FY12, on the strength of their comparatively superior service levels, product innovation, customization and targeting of specific client segments not addressed by banks
- HFCs to be included as eligible borrowers for financing low cost housing projects through ECBs, which should help in funding
- Regulatory initiatives for customers, like removal of prepayment penalty and uniformity in rates for old and new clients

Q3 FY14 performance | Consolidated financials | Business snapshots | **About us** | Thematic series | Industry facts

Group profile and structure

- Well-diversified, financial services company offering a range of financial products and services
- Focused on wealth creation for all its customers, such as institutional clients, HNWIs and retail customers
- Network spread over 519 cities comprising 1,546 business locations operated by our business partners and us with 792,858 total registered customers
- Shares listed on the Bombay Stock Exchange and National Stock Exchange in Mumbai

Motilal Oswal Financial Services Ltd.

99.95%	100%	85%	99.95% #	99.95% #	99.95% #	97.55%
Motilal Oswal Securities Ltd.	**Motilal Oswal Investment Advisors Pvt. Ltd.**	**MOPE Investment Advisers Pvt Ltd.**	**Motilal Oswal Asset Management Co. Ltd.**	**Motilal Oswal Wealth Management Pvt. Ltd.**	**Aspire Home Finance Corporation Limited**	**Motilal Oswal Commodities Broker Private Ltd.**
Institutional Equities Broking & Distribution	Investment Banking	Private Equity Real Estate	PMS Mutual Funds Offshore Funds	Financial Strategy Wealth Management	Proposed Housing Finance	Commodity Broking

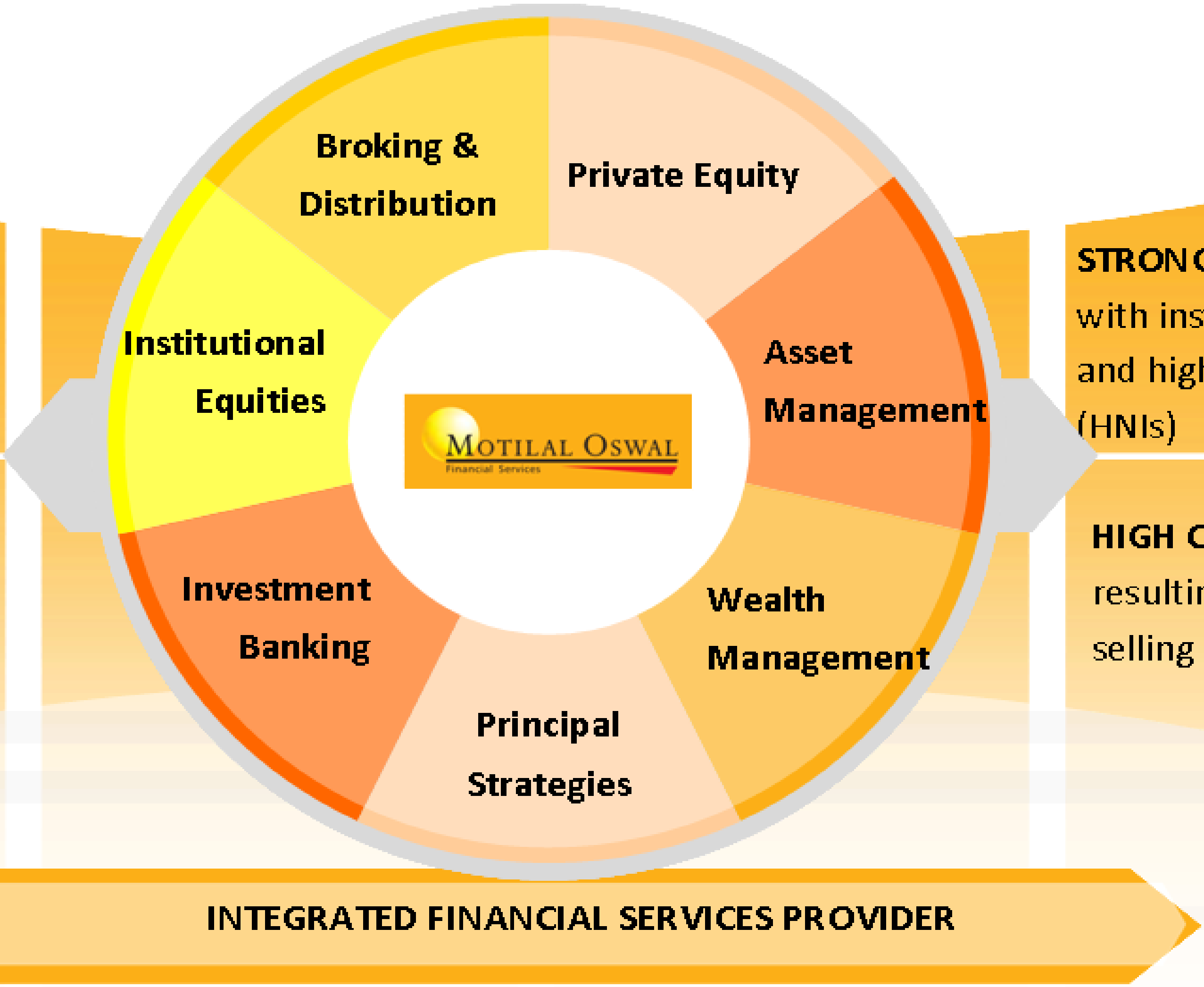
 # through Motilal Oswal Securities Limited

Data as on Dec 2013

Our businesses

Independent and
INSIGHTFUL RESEARCH

Well established
DISTRIBUTION NETWORK



STRONG RELATIONSHIPS with institutional investors and high net worth investors (HNIs)

HIGH CREDIBILITY resulting in higher cross-selling opportunities

Our driving force

Time bound results within the framework of the company's value system

A company honoring commitment with highest ethical and business practices

High energy and self-motivated with a "do it" attitude and entrepreneurial spirit

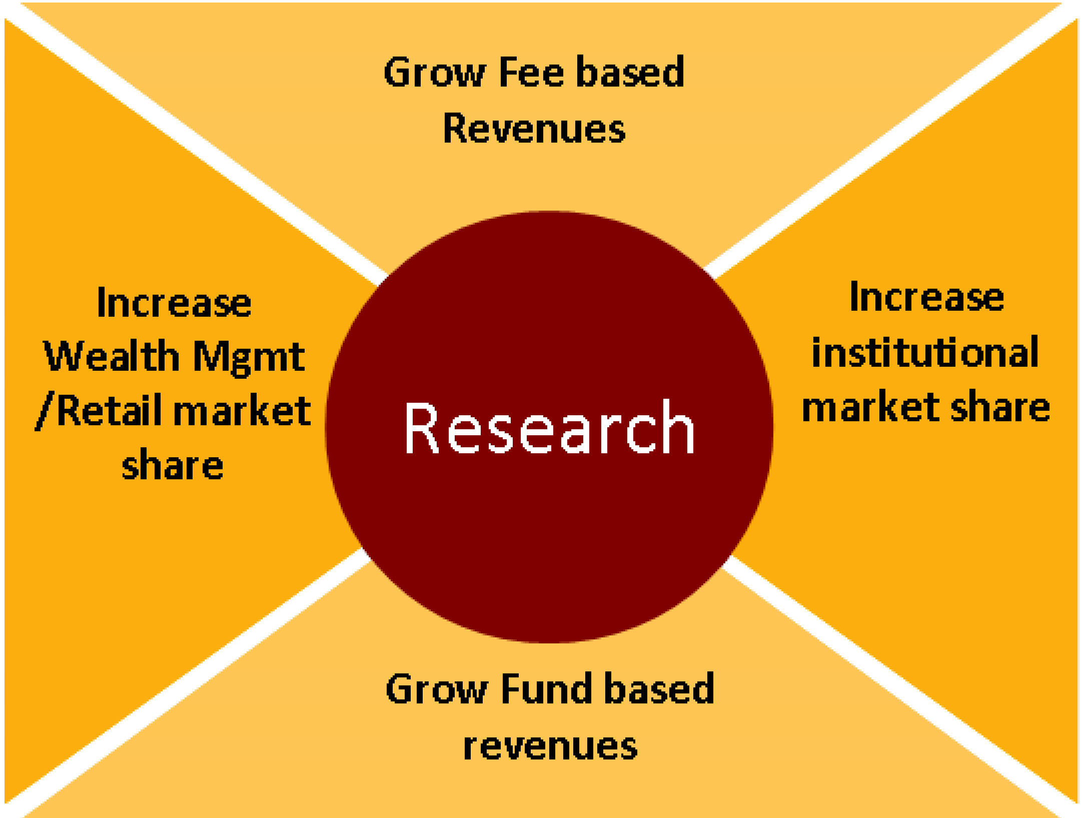
Attaining goals collectively and collaboratively

Performance gets differentiated, recognised and rewarded in an apolitical environment

Our business strategy

- Grow Investment banking business
- Build Asset management and Private equity business

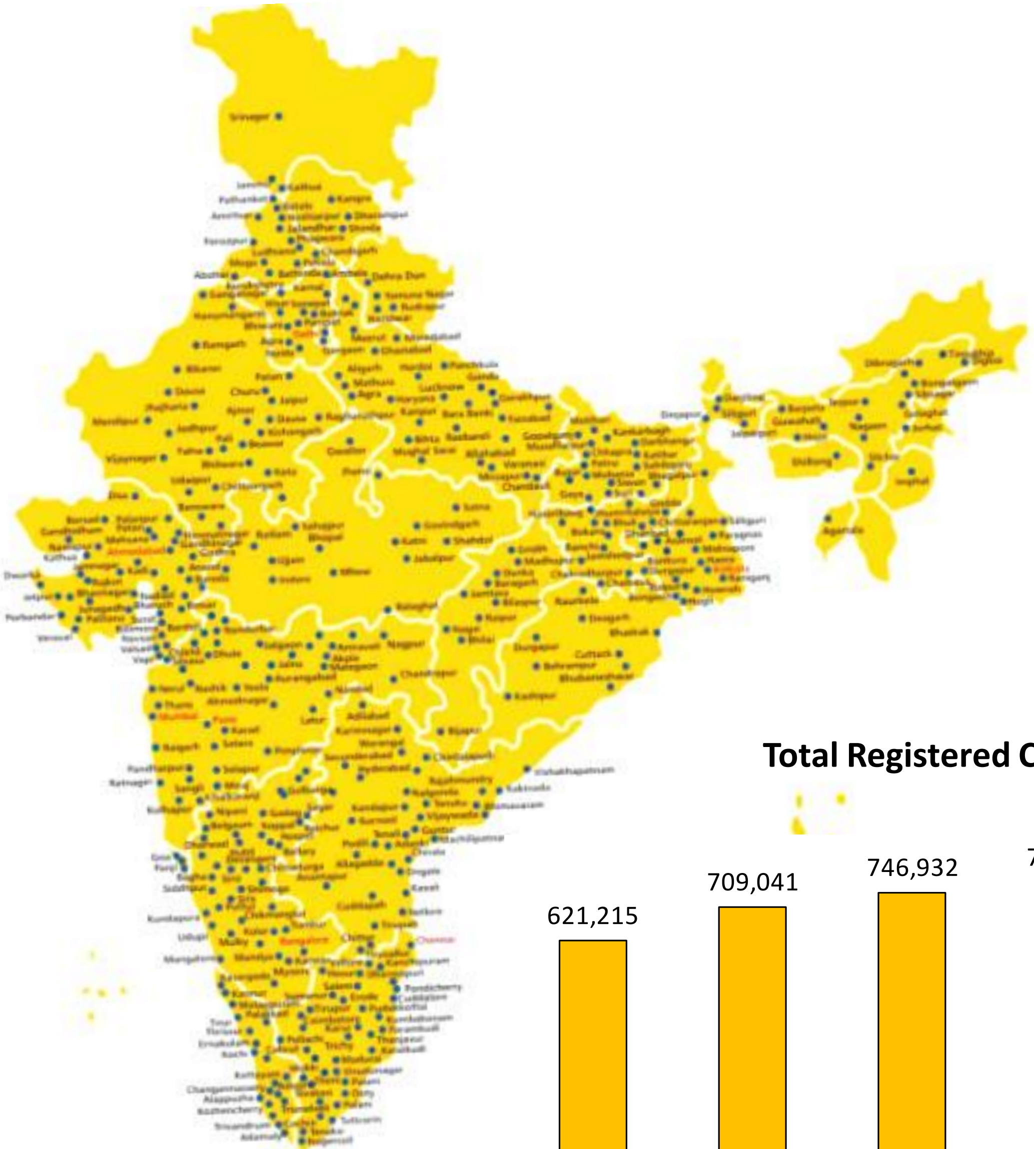
- Strong distribution network across India
- Leverage research and advisory capability
- Create products suited to customer needs
- Increase distribution of third party products



- Build stronger institutional relationships through wider and quality research
- Increase research support
- Grow institutional derivatives business

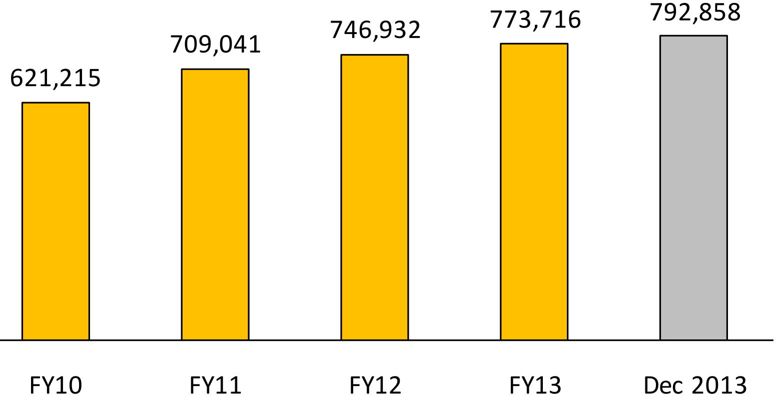
- Principal Strategies Group to maximize returns using risk free arbitrage strategies
- Grow capital market related lending business

Pan-India distribution network

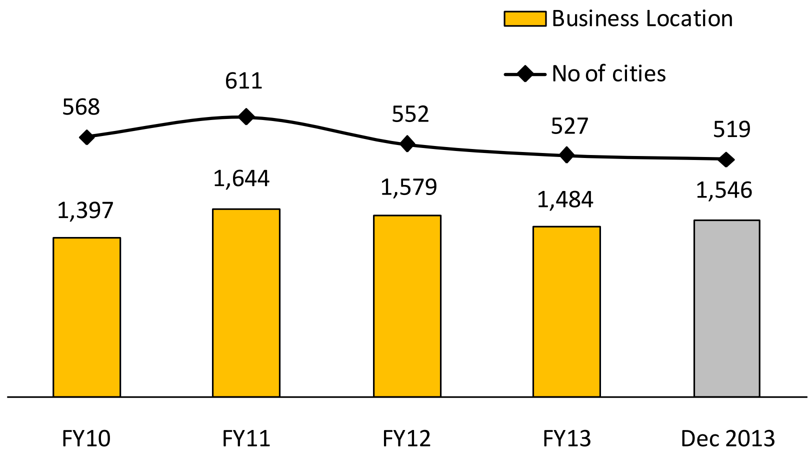


- Pan-India network with a presence in 519 cities across 1,546 business locations (branches plus franchisees), and complemented by a robust online channel
- Total registered client base of 792,858 which includes 695,663 retail broking and distribution clients
- Robust distribution network providing opportunities to cross-sell products, particularly as we diversify further into new business streams

Total Registered Clients



Distribution (Business Locations & Cities)



Award winning research and sales teams

Focused Research team

- Strong research team comprising over 30 research analysts covering over 200 companies across 20 sectors and 27 commodities
- Focused on cash equities, equity derivatives and commodities and services all our business segments

Strong Sales and Corporate Access Team

- Research supported by an extremely strong sales trading team comprising of qualified professionals
- Conducts a number of corporate access events throughout the year. Its Annual Investor Conference is one the largest event formats of its kind in this industry

MOSL has been consistently ranked amongst the top brokerage houses for its research

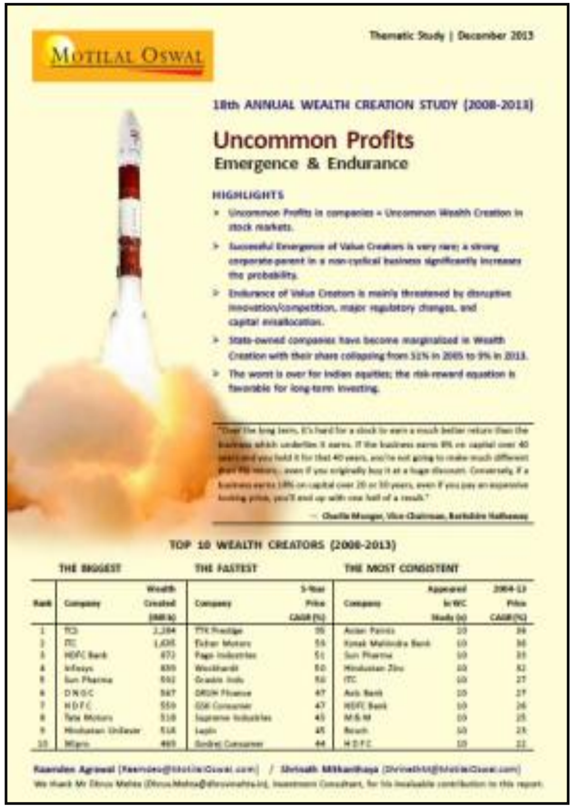
ET Now Starmine Analyst Awards 2010-2011

Award Winning Categories:

Category	Sector	Rank
Top Earnings Estimator	Across Sectors	1
Top Earnings Estimator	Financials	1
Top Stock Picker	Energy	1
Top Stock Picker	Real Estate	2

Annual Wealth Creation Study

MOFSL conducted its 18th Annual Wealth Creation Study in December, 2013 on the topic “Uncommon Profits: Emergence and Endurance”. The presentation of the study was followed by a Panel Discussion.


Thematic Study | December 2013

MOTILAL OSWAL

18th ANNUAL WEALTH CREATION STUDY (2008-2013)

Uncommon Profits

Emergence & Endurance

HIGHLIGHTS

- Uncommon Profits in companies = Uncommon Wealth Creation in stock markets.
- Successful Emergence of Value Creators is very rare; a strong corporate-parent in a non-cyclical business significantly increases the probability.
- Endurance of Value Creators is mainly threatened by disruptive innovation/competition, major regulatory changes, and capital misallocation.
- State-owned companies have become marginalized in Wealth Creation with their share collapsing from 51% in 2005 to 9% in 2013.
- The worst is over for Indian equities; the risk-reward equation is favorable for long-term investing.

— Charlie Munger, Vice Chairman, Berkshire Hathaway

TOP 10 WEALTH CREATORS (2008-2013)

	THE BIGGEST		THE FASTEST		THE MOST CONSISTENT		
Rank	Company	Wealth Created (INR b)	Company	5-Year Price CAGR (%)	Company	Appeared in WC Study (x)	2008-13 Price CAGR (%)
1	TCS	2,284	TTK Prestige	[illegible]	Asian Paints	10	[illegible]
2	ITC	1,635	Eicher Motors	[illegible]	Kotak Mahindra Bank	10	[illegible]
3	HDFC Bank	873	Page Industries	[illegible]	Sun Pharma	10	[illegible]
4	Infosys	839	Wockhardt	[illegible]	Hindustan Zinc	10	[illegible]
5	Sun Pharma	[illegible]	[illegible]	[illegible]	ITC	10	27
6	ONGC	[illegible]	GRUH Finance	47	Axis Bank	10	27
7	HDFC	[illegible]	GSK Consumer	47	HDFC Bank	10	26
8	Tata Motors	[illegible]	Supreme Industries	[illegible]	M&M	10	[illegible]
9	Hindustan Unilever	[illegible]	Lupin	[illegible]	Bosch	10	[illegible]
10	Wipro	[illegible]	Godrej Consumer	44	HDFC	10	[illegible]

- Identified TCS, TTK Prestige and Asian Paints as the biggest, fastest, consistent wealth creators
- It showed that 7 of the Top 10 Wealth Creators during 2008-13 were non-cyclicals
- Wealth creators defy the common maxim “high return, high risk". At the time of purchase, the P/E of wealth creators is lower than benchmark (i.e. lower risk), and yet the returns are higher
- Technology sector is poised to emerge as India's largest Wealth Creator in the near future
- Many young companies have emerged in the value creation zone, led by a good management

Theme of this study was on **‘Uncommon Profits: Emergence and Endurance’.** Key takeways were:-

- Uncommon Profits in companies = Uncommon Wealth Creation in stock markets
- Successful emergence of value creators is very rare; a strong corporate-parent in a non-cyclical business significantly increases the probability
- Endurance of value creators is mainly threatened by disruptive innovation/competition, major regulatory changes, and capital misallocation
- State-owned companies have become marginalized in Wealth Creation with their share collapsing from 51% in 2005 to 9% in 2013

The 18th Wealth Creation report can be downloaded by clicking on this link http://www.motilaloswal.com/Wealth_Creation_Study/Studies/

Mr Motilal Oswal – CMD, MOFSL and Mr Raamdeo Agrawal – Jt MD, MOFSL with Panel Members: Mr Kenneth Andrade – Head Investments, IDFC Asset Management, Mr Anil Singhvi – Chairman, Ican Investors and Mr Sanjoy Bhattacharyya – Founder, Fortuna Capital

Q3 FY14 performance

Consolidated financials

Business snapshots

About us

Thematic series

Industry facts

"Affordable housing finance in India – The emerging opportunity and its critical elements"

- Housing is a key multiplier in the nation's economic growth, given its linkages with numerous ancillaries
- In terms of housing finance, majority of loans disbursed have been to the high/mid-income groups due to easier availability of proofs for credit assessment. Affordable housing finance is now a focus area of the Government as well
- While the Government estimates the national housing shortage at ~19mn, Monitor Inclusive Markets pegs the shortage at ~22mn for budget homes priced between Rs 0.3-1mn and ~5mn for homes priced between Rs 1-2.5mn
- This spells a potential home loan opportunity of ~Rs 8-22tn (assuming a lower LTV of 65-70% since HFCs might demand higher commitment from this borrower segment). While this is a long term estimate, even if an inventory of 1mn out of this actually hits the market in the next few years, it means a potential loan opportunity of ~Rs 300-800bn
- Moreover, the sizable inventory expected to come up in this segment indicates a significant opportunity for HFCs. With only the surface of this segment being scratched by financiers so far, we refer to this as an 'iceberg' scenario

Most housing development so far has largely targeted the high and mid-income population due to easier availability of proofs for credit assessment. There remains a glaring gap between supply and demand for the mid/low-income and informal sector – the Affordable Home segment

Identifying this target borrower…

- Affordable housing roughly refers to dwellings of 250-800 sq ft area and below a price of Rs 2.5mn. Assuming housing costs to be typically ~33% of household income and average tenure of 20 years, it indicates households with monthly income within Rs 12,000-60,000
- This includes mid/low-income population earning from salary and self-employment. Most are first-time home buyers with numerous queries related to purchasing/financing process
- There are perceived risks associated with lending to these people. Nevertheless, most are genuine home-buyers and committed to repaying their loans, since they would gladly exit their current housing options – which are poorly constructed, with poor sanitation/support-infrastructure and poor social environment for children

There is already an available buyer base and HFCs do not really have to create demand. They instead need to ensure appraisal and collection processes function optimally without slippages

Please click here: http://www.motilaloswal.com/Financial-Services/Investor-Relations/Presentation

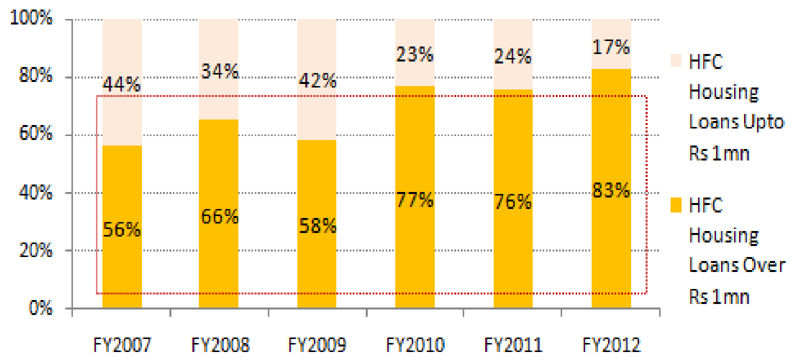
Where are the potential target markets…

- The opportunity exists in large cities like Mumbai, Bangalore, Delhi, and Industrial-Corridors like Delhi-Jaipur and Kalyan-Karjat. Ahmedabad, Indore, Chennai, Jaipur, Nagpur, Baroda are evincing interest, which is encouraging
- 30,000+ units have already been constructed from Jun 2011 to Jan 2013. Of this, ~30% are priced below Rs 0.6mn. With VBHC and TATA's Shubh Griha etc announcing projects, the supply run-rate is expected to pick up
- With the uptick in development, the momentum in affordable housing finance has gained pace. New entrants have joined the earlier incumbents. Most new players are regional-focused with operations centered around few states bordering each other. These are typically states with a large population base (to scale up business from fewer locations). Tamil Nadu, Gujarat, Maharashtra, Bihar, Rajasthan, AP, WB, UP are examples. Some micro-housing HFCs have also come up to serve the informal-low income niche specifically
- There is more demand for the 1RK format in Mumbai, Ahmedabad, while 1/2BHK formats are popular in Indore, Jaipur etc. Developers also see opportunity in mixed-income projects as they get sold faster

Initial buyer response has been encouraging. Some developers are now in their 2nd or 3rd round of projects, and plan to enter Tier 2/3 markets too – a positive sign since it means the commercial viability exists

Given Indian cities' space constraints, customers are seen to prefer the format of more rooms vs. larger rooms

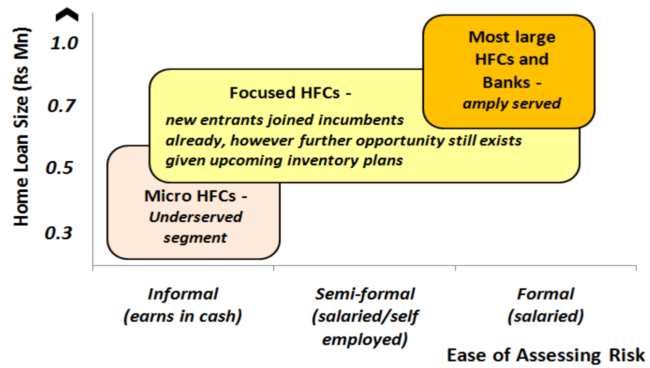
So far, HFCs' housing loans to individuals have remained skewed towards the >Rs 1mn loans, as the focus has been more here…



…as a result, the CAGR in the >1mn category has also been higher

	5 Year CAGR
Upto Rs 0.5mn	-17%
Btwn Rs 0.5-1mn	14%
Over Rs 1mn	32%
Overall	**23%**

HFC market map and opportunities, based on the loan amount and client category served



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Operational criticalities…

- **Field-based credit assessment:** Risk assessment is complicated for self employed and informal categories. Self employed borrowers often do not have consistent monthly income as their earnings are prone to business cycles, and the income capability of each is different. Hence, credit assessment processes needs to be dynamic. HFCs may use field-based credit assessment by visiting the client personally to understand the nature of his work, income flow patterns, monthly commitments, savings, his attitude/lifestyle, the loan's objective and collect documents. The officer needs to do cross-reference checks by meeting the applicants' customers, creditors, suppliers and competitors to gauge a reasonable profit generated by his business. Field officers should be able to gauge the client's repayment capabilities and his genuine willingness to repay
- **Retaining quality credit appraisal staff and training fresh recruits:** Credit officer's role is critical, and experienced ones with good strike-rates might claim a premium. HFCs might need to benchmark best-practices which can help train fresh recruits who come at a lower price
- **Early-warning systems in collection:** Repayment frequency can be weekly, fortnightly or more than monthly. MIS systems need to identify slippages through early-warning systems. This can ensure better monitoring of cash flows and faster turnaround for recovery in case of default
- **Marketing methods closer to the 'horse's mouth':** Affordable HFCs base home-loan counselors at the project site itself. Other methods include radio/newspaper/online advertising as well as banners behind buses/autorikshaws as these can best grab the eyeballs of their relevant target
- **Project risk:** HFCs need to house legal and technical officers to do checks on the property to ensure it is free of litigation, encumbrance etc. Not only does this help the HFCs to identify clean projects, but it also gives the comfort factor to the potential home-buyers
- **The Maths – a 'game of scale':** Given the complicated appraisal process in this segment, it can mean higher opex proportion and lower margins as compared to other HFCs. Hence, this is a business of scale – where higher volumes would compensate for lower margins. However, the chase for volumes cannot be at the cost of asset quality, which is where the credit officers' skills holds key. Typically, assuming HFCs to access debt from banks at rates in the range of 11-13%, it means the HFC would lend at 14-16% to earn a spread of 3% or thereabouts.
- **Operating structure – 'hub and spoke' preferred:** The corporate office divides its target geography into regional units, which are responsible for that area's branches. Regional office will house appraisal and collection staff, and operational team to process the paperwork. The branches will interact with the client and house credit appraisal and customer service staff. This hub and spoke structure helps maintain accountability of operations yet ensures faster turnaround as compared to structures where everything is routed centrally from the corporate office
- **Guarantor:** Guarantor is important, especially while lending to the informal sector. It mirrors the rationale behind using the group concept in microfinance as a proxy for collateral. An HFC is also working with reputed lenders to provide loan programs based on partial-guarantees.

Challenges and conclusion…

- Access to low-cost funds and the cost of debt is a major challenge to grow the book
- Demand for home finance might be impacted if there are more ‘pure investors’ purchasing homes rather than ‘genuine home-buyers’
- Credit risk assessment, retention of quality credit staff, early warning systems for default monitoring/follow-up are operational challenges
- Higher servicing costs due to more involved nature of credit appraisal
- Ability to build scale ahead of competitors to ensure profitability in a high opex scenario
- Lower appreciation/liquidity in small towns can lead to difficulty in sale during recoveries
- Timely completion of projects without cost escalations is a key concern
- Ability to build an enabling environment via faster approvals, support-infrastructure, etc

Financial service firms who seek to offer an entire gamut of products need to view housing as an essential credit product, as it is a long-duration relationship during which it can sell more products to that captive base, provided the client’s experience during the home loan process was positive

In conclusion, the residential piece constitutes the bulk of the Indian real estate market and affordable housing is set to be a major driving segment in this. While the supply of affordable housing and finance has increased, the gap between supply and demand is still huge, spelling a significant opportunity. Excellence in operational processes like appraisal/collection hold key to the business’ success. Access to lower-cost funding and the ability to build scale is a chicken-egg story, since money will not flow to them till they have capacity and without funding, they cannot develop. Tapping the capital markets for funding is a substitute to bank funds, however the ability to deepen the usage of capital markets will require closer collaboration between the HFCs, government, rating agencies and investors.

Please click here to read the full article, plus access previous Fin-Sight articles:
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Q3 FY14 performance

Consolidated financials

Business snapshots

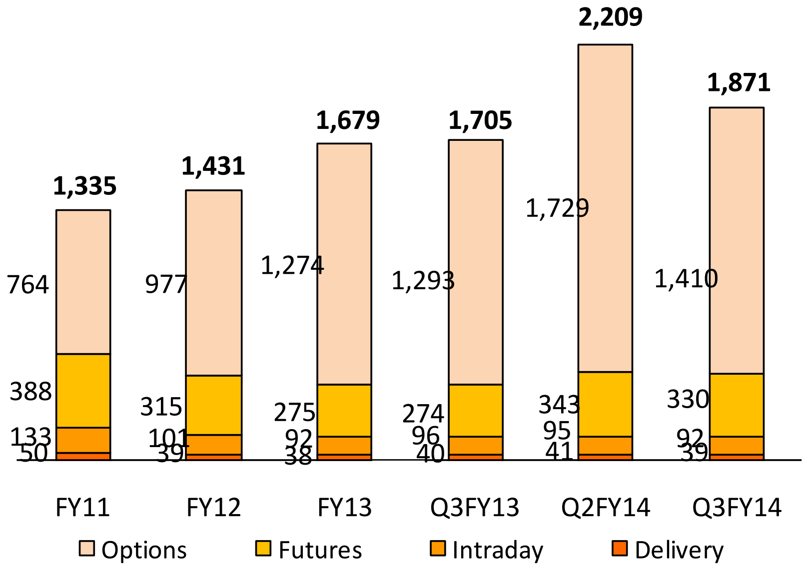
About us

Thematic series

Industry facts

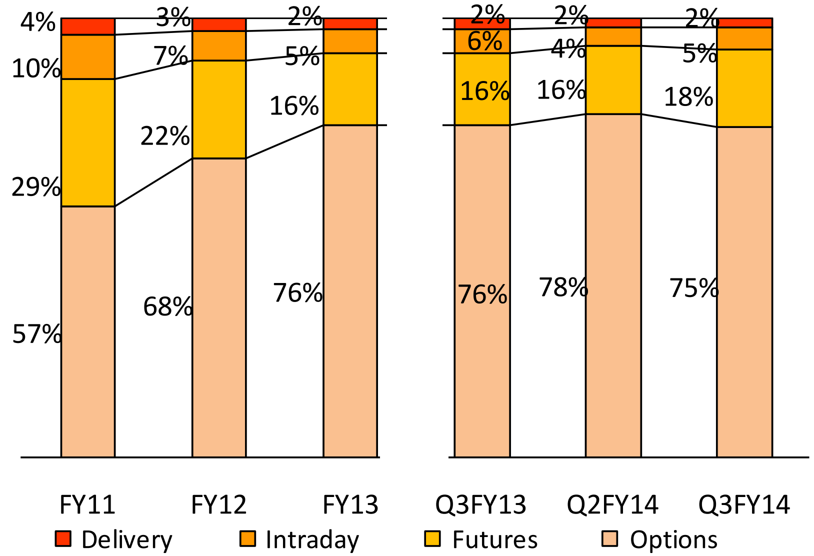
Options dip QoQ in Market ADTO; Cash/delivery slightly down

Market ADTO saw a QoQ dip due to lower volumes clocked in options; Overall cash and cash delivery also dipped slightly (Rs Bn)



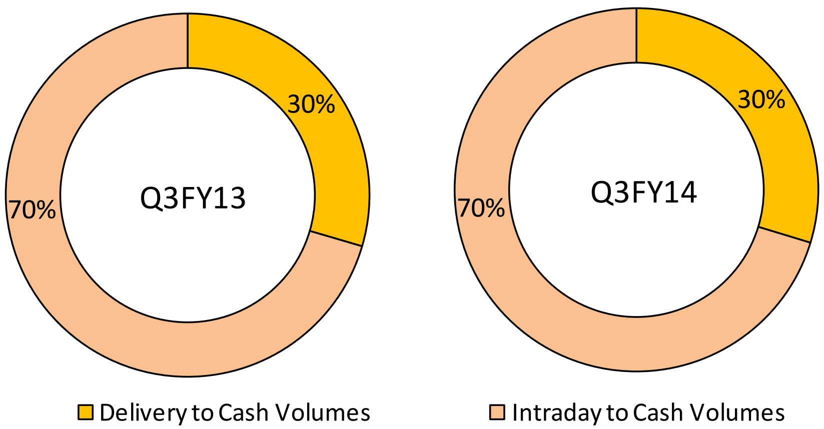
Source: NSE, BSE

With lower option volumes on a QoQ basis, the proportion of options was slightly lower, while cash proportion saw an uptick



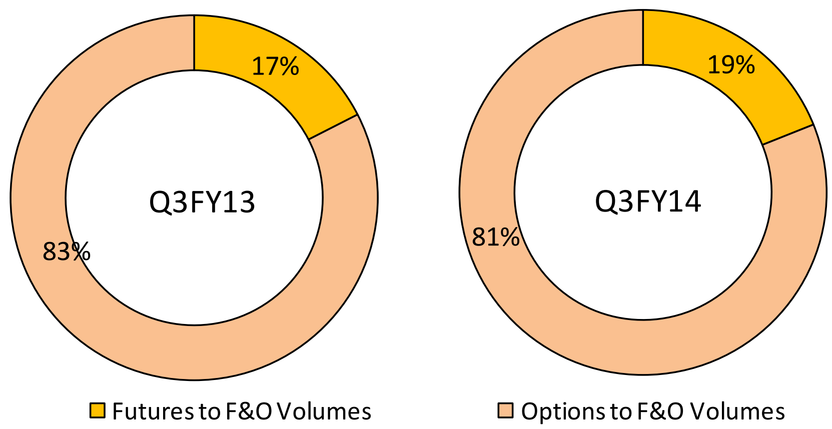
Source: NSE, BSE

On a YoY basis, the proportion of delivery within cash volumes in the market has held steady at 30%



Source: NSE, BSE

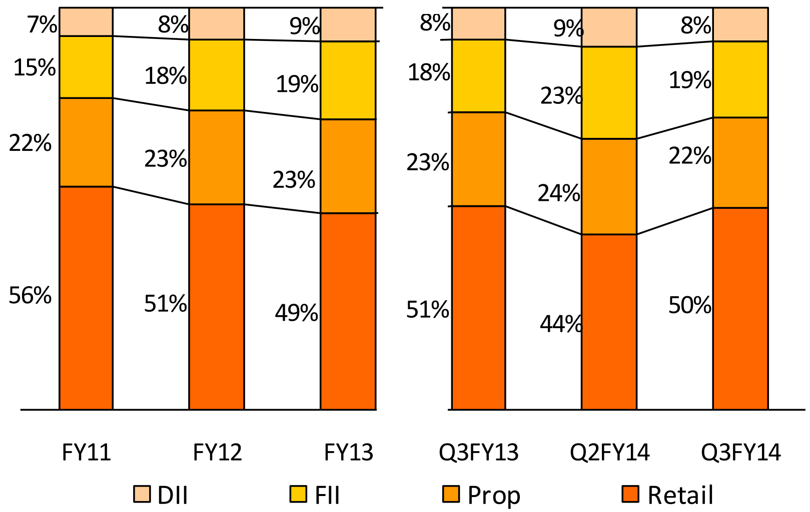
Proportion of options within F&O in the market has tapered slightly owing to lower option volumes



Source: NSE, BSE

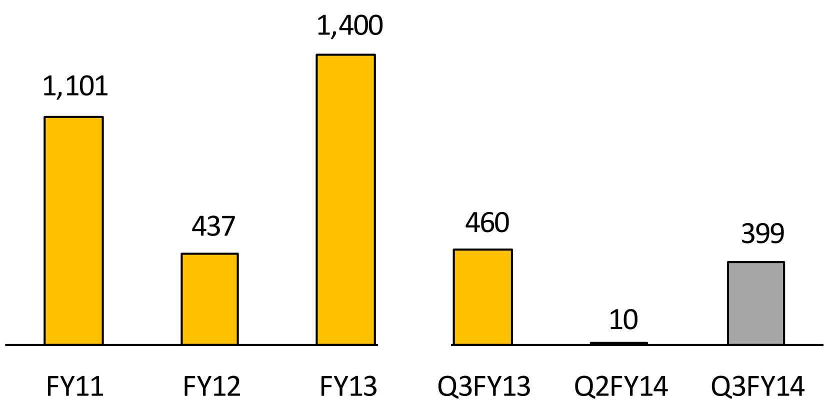
Retails' percent picks up in Cash ADTO; FII inflows see uptick

Retail's proportion within cash volumes has increased on a QoQ basis, while that of FII and Prop segments dipped



Source: NSE, BSE

After seeing net outflows from equities during the months from Jun to Aug, net inflows picked up in Q3FY14 owing to strong inflows clocked in Oct and Dec months (Rs Bn)

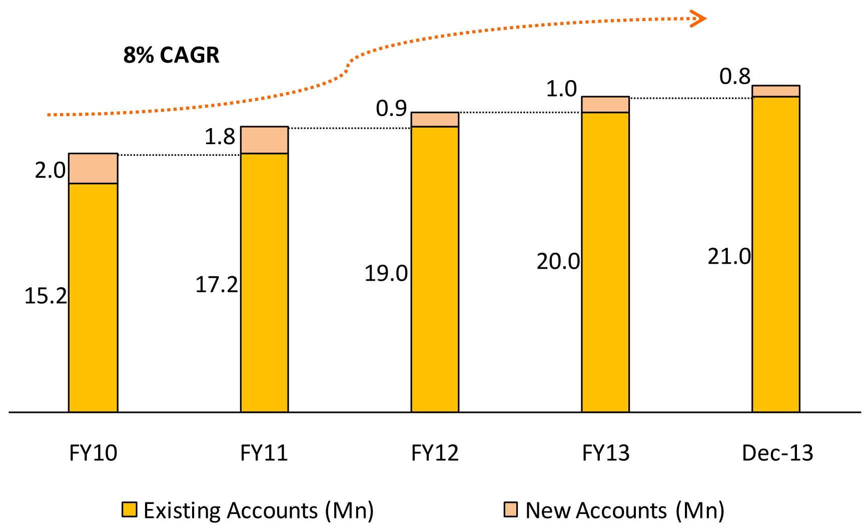


Source: SEBI

DIIs have seen net outflows from equities since the last 6 consecutive quarters; The outflow clocked this quarter was much higher than earlier quarters, except for 4QFY13 (Rs Bn)

Source: NSE

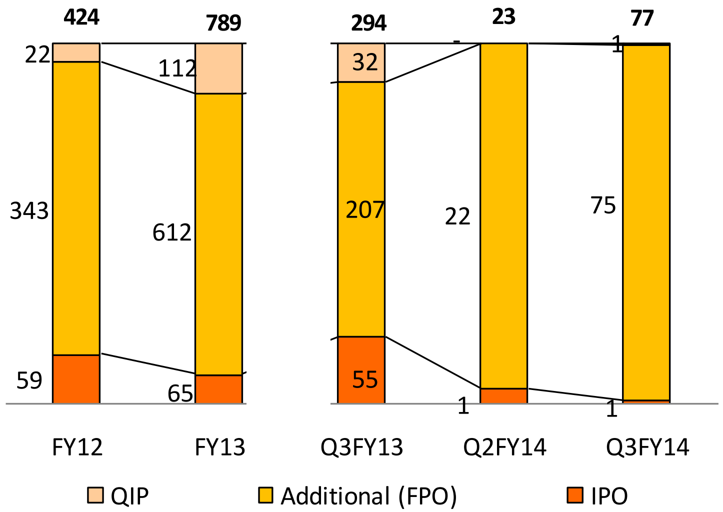
Growth in new demat accounts (Mn) remains low, as primary market activities have largely dried up



Source: CDSL, NSDL

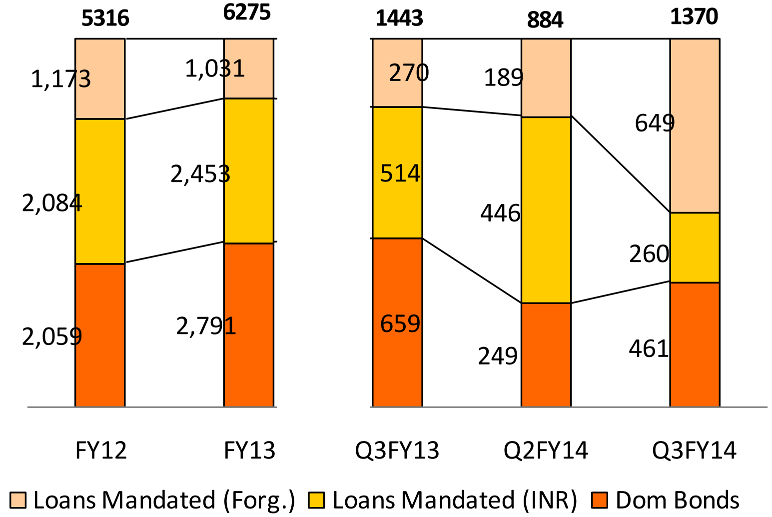
Though still sluggish, ECM, DCM, M&A & PE post slight QoQ uptick

ECM activity showed a marginal QoQ uptick as the Powergrid FPO issue boosted the Additional segment; However, ECM continues to remain dry as compared to earlier years (Rs Bn)



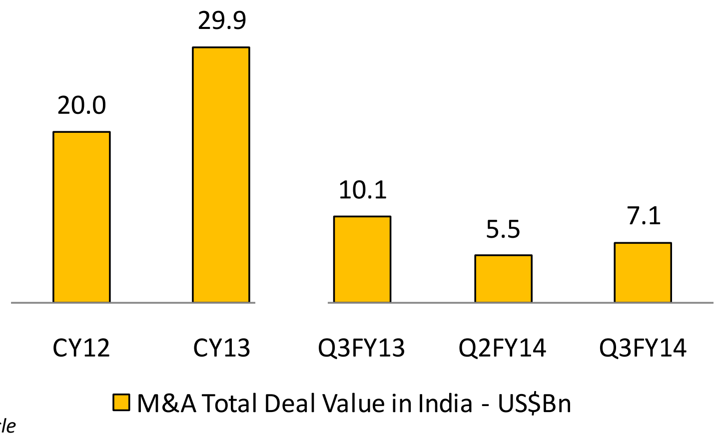
Source: Bloomberg, BSE (for QIP)

DCM saw a slight uptick on a QoQ basis buoyed by increase in domestic bond issues and foreign loan segment (Rs Bn)



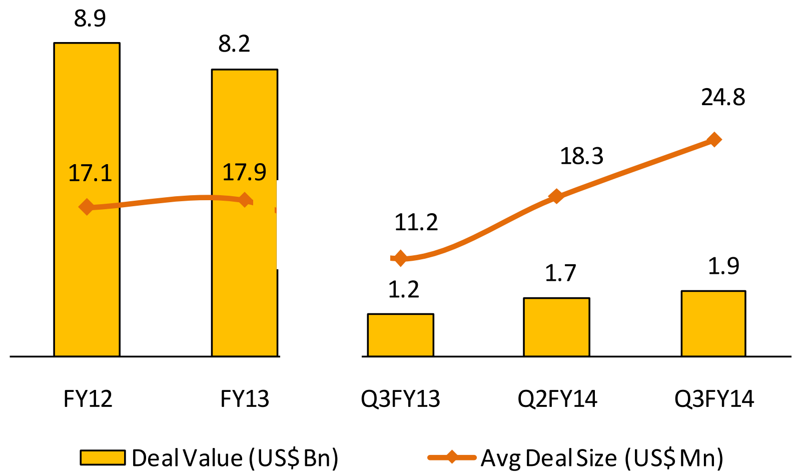
Source: Bloomberg

M&As deals picked up slightly this quarter on a QoQ basis; On a CY basis, cross-border deals saw increased activity while domestic deals saw a drop; Energy, power, healthcare, industrials and telecom clocked the highest % of deals in CY13 (US$Bn)



Source: Thomson Reuters news article

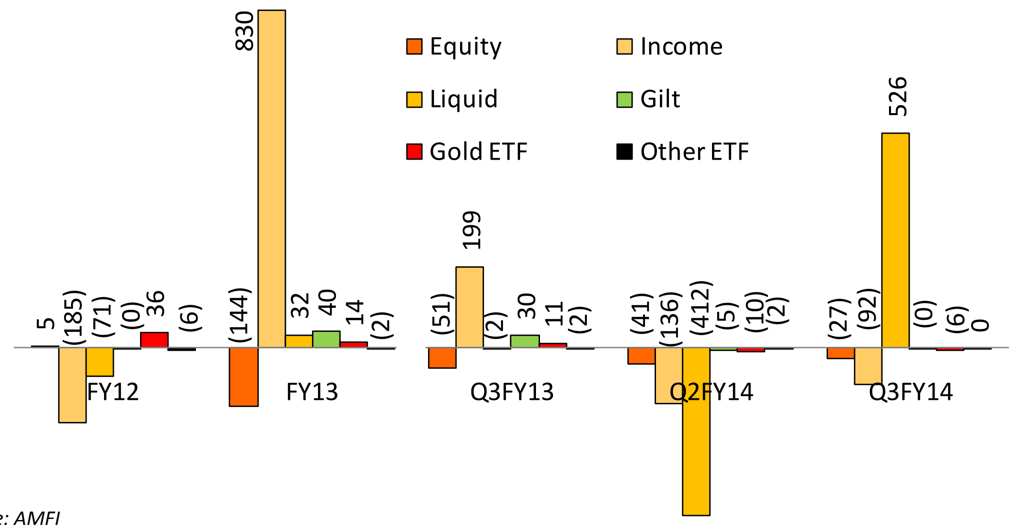
PE deal value picks up QoQ and YoY, largely due to the $420mn Global Logic-Apax Partners deal; Average deal value picked up as high-value deals were scarce in recent quarters (US$Bn/Mn)



Source:: Venture Intelligence

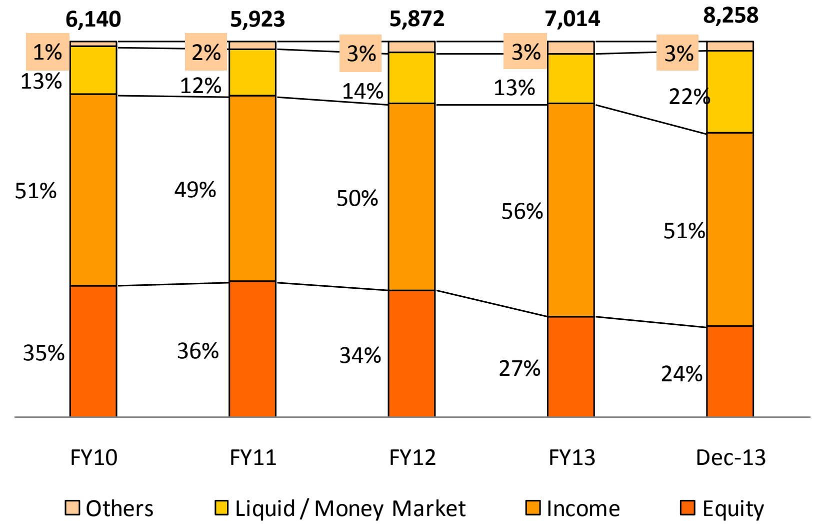
Redemptions hit most MF segments; Liquid props up MF AUM

Redemptions seen in all segments in Q3 FY14 except in Liquid; Equities seen net outflows in last 8 consecutive quarters (Rs Bn)



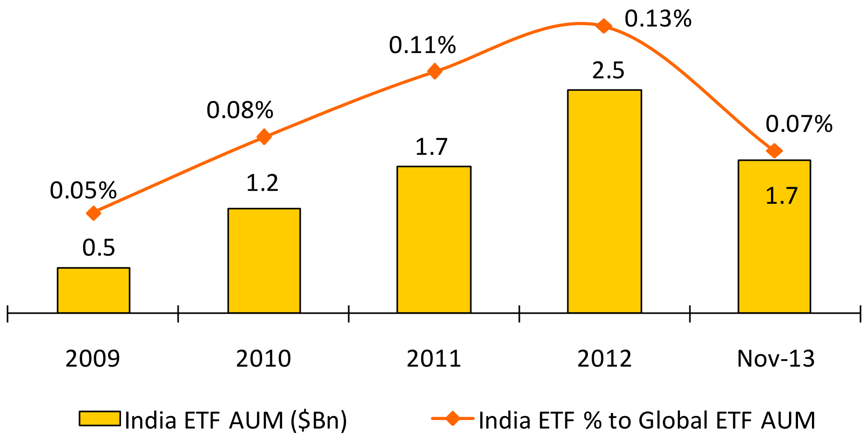
Source: AMFI

Liquid funds have led the MF AUM growth on a YTD basis; Income and Equity saw slight growth; Dips in Gilt and Gold lowered Others



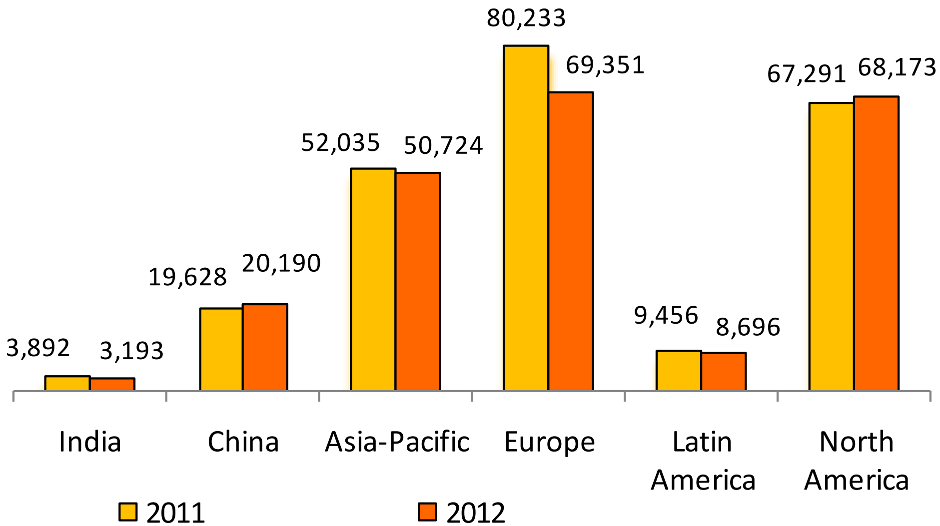
Source: AMFI

Decline in Gold ETF AUM has lowered the Indian ETF assets on YTD basis; Non-gold ETF assets also dipped marginally (US$Bn)



Source: AMFI/Blackrock report

India's economic slowdown has impacted its Total Net Wealth in 2012 vs 2011 (US$ Bn); While China has held its ground, net wealth has also declined in 2012 in the broader Asia Pacific region



Source: Hubbis report

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Thank You

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