"Cholamandalam Financial Holdings Limited

Q2 FY '25 Earnings Conference Call"

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MANAGEMENT: **MR. SRIDHARAN RANGARAJAN – NON-EXECUTIVE DIRECTOR – CHOLAMANDALAM FINANCIAL HOLDINGS LIMITED**
MR. N. GANESH – MANAGER AND CHIEF FINANCIAL OFFICER – CHOLAMANDALAM FINANCIAL HOLDINGS LIMITED
MR. V. SURYANARAYANAN – MANAGING DIRECTOR – CHOLAMANDALAM MS GENERAL INSURANCE COMPANY LIMITED
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MODERATOR: **MR. PARTH JARIWALA – DAM CAPITAL ADVISORS**

Moderator: Ladies and gentlemen, good day, and welcome to the Q2 FY '25 Earnings Conference Call of Cholamandalam Finance Holdings hosted by DAM Capital Advisors. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the call, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Parth Jariwala from DAM Capital Advisors. Thank you, and over to you, sir.

Parth Jariwala: Thank you. Good evening, all. Welcome to Q2 FY '25 Earnings Call of Cholamandalam Financial Holdings Limited. From the management, we have Mr. Sridharan Rangarajan, Non-Executive Director, Cholamandalam Financial Holdings Limited; Mr. N. Ganesh, Manager and Chief Financial Officer, Cholamandalam Financial Holdings Limited; Mr. V. Suryanarayanan, Managing Director, Cholamandalam MS General Insurance Company Limited; Mr. S. Venugopalan, Chief Financial Officer, Cholamandalam MS General Insurance Company Limited.

I'll now hand over the call to management for their opening remarks and post which we can open the floor for question and answers. Over to you, sir.

Sridharan Rangarajan: So good afternoon to all of you, and thanks for participating in our call. I would request Mr. Suryanarayanan, MD of Cholamandalam MS to cover the insurance business as the NBFC business is well covered, and you have seen already the presentation, would have attended the call. So I would request Sury to talk about chola MS .

V. Suryanarayanan: Thanks, Sridhar. Good evening to all of you who have joined this conference call of Chola Financial Holdings. I shall now proceed to give an overview of the performance of Chola MS both for the quarter and the half year. In Q2, Chola MS recorded a gross direct premium of INR2,171 crores, with a growth rate of 9.2% as against the multi-line insurers growth of 1.7%.

As at the half year, the top line was at INR4,092 crores with a growth rate of 11.5% as against the multiline insurers growth at 6.7%. In this quarter, the company grew higher than industry in motor, fire and miscellaneous lines of business. In group health, the company grew its volume to INR233 crores for the half year, which volume still is one of the lowest amongst multiline players.

As at the half year, the composition of motor has reduced to 59% from 62% in the corresponding period. In motor, which is the principal line of business, the growth in the quarter was at 10.6% as against industry growth of 6.2%.

The company presently has a composition of 40% in cars, 43.8% in commercial vehicles and 16% in 2-wheelers. And the company gets about 29% of its total motor premium from new vehicles. During the quarter, the company added a few large NBFC partners.

Moving on to the expenses of management. The percentage for Q2 was 32.18% as against 29.7% in the corresponding quarter. As at the half year, it was at 32.73% as against the previous full year of 32.71%, which means more or less flat as compared to the previous full year.

In the half year, the company has expended INR56 crores towards technology spend as against INR37 crores in corresponding half year. This tech spend has also contributed to the higher EOM. The claims ratio was at 72.6% as against 73.8%, lower by about 1.2%. This quarter, we had the NAT CAT events by way of flood and inundation in Andhra, Telangana and Surat, which impacted the company for an amount which was very similar to the impact that the company had the corresponding quarter of previous years.

The company continues to be prudent in its reserving for motor third-party claims. Chola MS investment portfolio corpus as at September was at INR17,189 crores, and we had an investment income of INR342 crores for the quarter. The PBT in the quarter and half year were at INR171 crores and INR350 crores. This included nonrecurring income of INR22.68 crores by way of interest on income tax refund.

Our return on equity for the half year progressed to 10%, not annualized, the solvency was at 2.06x. The company has been progressing on several digital initiatives. We had the migration of the private car portfolio from the legacy ERP systems to a cloud architecture with the contemporary configuration capabilities and micro services-based API. The company will be embarking on the next Phase of migration in this quarter.

We'll now be happy to take any questions that you may have.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Atul Mehra from Motilal Oswal.

Atul Mehra: I have asked this question before in the earlier calls. Just wanted to check again on what is the path towards more value realization for shareholders of Chola Financial Holdings? Because I think in the number of conversations we have had in the past, we've discussed of this particular matter. So if you could update on what the Board is thinking about this and as shareholders what should we expect?

Sridharan Rangarajan: So thank you for your persistent asking this question. As earlier communicated, the Board has not considered this aspect. But definitely, it would take an appropriate call at an appropriate time. So at this point in time, no such discussion has happened.

Atul Mehra: Right. Sir, can we have any communication from the Board with this particular matter? Because obviously as a shareholder, this is of most importance to us. So can we expect -- or can you, through this conversation table this as a matter of discussion so that we have more clarity on this aspect?

Sridharan Rangarajan: I think definitely, the Board is seized of what is happening, what is the development in the market. And definitely, it would take an appropriate call at the time which is suitable and it feels comfortable. So I think that's what we could communicate to you at this time.

Moderator: The next question is from the line of Sanketh Godha from Avendus Spark.

Sanketh Godha: Sir, when I look at 1H to 1H, our loss ratio has improved except catastrophe event also by 130 basis points. But somehow, our opex ratio, which was 36.3% last year, has increased to 37.4%, and that has been a bit of drag on commensurate improvement in the combined ratio. So just wanted to understand, going forward, how do we see this opex ratio to play out given [inaudible 0:10:06] is around and the combined trajectory to play out? That's on overall cost.

And second question is predominantly on motor. See, we see that most of the lines have seen a bit of improvement in the loss ratios, maybe if I exclude the cat events. But Motor OD seems to be a little higher compared to what historical comfort we used to give. Can I attribute this largely because our 2-wheeler component has gone up and the 74-point kind of motor loss ratio is the new normal if we continue to maintain the current product mix going ahead? So these are my 2 questions.

V. Suryanarayanan: Thanks, Sanketh. You are talking of 37%, which is not the EOM, which is the CoR component, which is net of the reinsurance commission, the sourcing cost minus what you are talking of. Let me tell you that our insurance commission recognition is fairly conservative. And we wait for the events to pan out before recognizing the full eligible reinsurance commission, which therefore can be better if there are no more events that come through in the subsequent periods. So that is one element which can improve the combined ratio going forward.

On the cost itself, I did mention in my opening remarks that we have had some tech spend which component will probably continue for H2 as well and probably H1 of next years. So this legacy system transformation plus whatever we are doing as part of our other multiple tech transformation programs will have this cost element, but I think we should look at it more from a future perspective.

And in any case, this expenditure will also qualify for the additional allowance that the regulator has spelt out for the Insurtech and other related spend. So that would be my view on the cost structure. On the pure opex structure, we compare favorably with most other competition.

Moving on to your second question relating to the Motor OD LR. If one were to just look at that Page 54, which shows the trend of the Motor OD LR over the period. And of course, this quarter, we have had higher Motor OD LR as compared to the past. Our mix is also you would notice that has a higher component of commercial vehicles.

And in commercial vehicles, we would -- we are present across the spectrum for the small, intermediate and the heavy commercial vehicles. And to that extent, our Motor OD loss ratios will be different as compared to certain other players. But what you will see is that over a period, so this is more or less stable. And generally, we have also seen that the loss ratios in H2 is always lower than H1 for multiple reasons and we are likely to see that trend as well.

So you mentioned about 2-wheelers, 2-wheelers, it's not a worry more on the OD side. 2-wheelers will be a worry more on the motor third-party side, particularly with the long-term in perspective and without the pricing correction, our companies would be hesitant to lock themselves in for the longer term at the current prices, even though we know that inflation will creep in by the time you reach the fourth or fifth year, both in terms of minimum wages as well as the medical inflation that will come.

Sanketh Godha: Got it, sir. With the one, we wrote 10 combined almost for first half. You delivered almost annualized 20% ROE. So just asking, given the trajectory will be better in the second half, I'm believing you might be -- maybe fair to say that your combined ratio in FY '26 or '27 will be much better than what it is today.

So is it fair that this 10% ROE for the half or annualized 20% ROE is now here to stay? Or do you see this number can be bit of -- I know there is a bit of one-off with respect to income tax reversal and all these things. But even that 18% to 19% ROE still, we believe is achievable, sir?

V. Suryanarayanan: Yes, you rightly called out the onetime, which would have given some basis points to this 10% non-annualized. But look, if you look at the trend over the quarters, you will find that things have only been improving, and I don't see any reason why this cannot be sustained.

Sanketh Godha: Okay, sir. And lastly, maybe just based on this long-term policy, which now is on -- which has to be recognized on [1xN ph 0:16:18] basis. Just if you can tell what is the exposure right now as on 1H FY '25? And given it's a very profitable book for us, how do you try to overcome the challenge with respect to this particular business going ahead, given you compete with the multiple players in open architecture banker channels and maybe indirectly you might be even competing with life insurance in this particular product. Sir, just want to understand your strategy, how you will go -- going ahead, conduct the business?

V. Suryanarayanan: Yes, good question. So this matter, of course, is being still pursued by the industry with the regulator though of course, the regulator has made it mandatory that the change will be effective from October. Nevertheless, the industry is still pursuing. What this does is that it's the accounting recognition that is changing from a top line perspective.

But from a cash flow perspective, the money will still come to the insurers. It is going to reflect in the investment corpus. And therefore, the investment income stream of things is not going to change in any way. The critical area of change is only going to be as to whether the cost will be paid upfront or whether it will be paid in the respective years.

So that is the dialogue that all insurers will be having with their respective industry partners. The dust has to settle down on that where the shape and the direction it ultimately takes is what will determine as to how things change.

But purely, on the investment income side, there is no change. If the companies are to pay upfront, which on the face of it looks like that is not permitted by the regulations, then you would have a lower reported top line and the cost being measured against that top line, which will mean that the expense of management will look bulged.

Sanketh Godha: But sir, given this is 1xN kind of a transition, then is it a fair assumption that if you -- regulator doesn't give any leeway on recognizing from 1xN then maybe you can expect a leeway on EOM compliance by, say, another year or so because anyhow the business will start flowing in and then there will be no incremental expenditure for the one which is booked already. Assuming you pay and the industry ends up with a practicing of paying upfront, then is it fair to say that some bit of leeway is expected to come from regulator on U.S.?

V. Suryanarayanan: What you're asking, I fully understand, but I don't know if I could make a guess on behalf of the regulator. I can't speak for the regulator. I'm sure as industry and as council, we will continue to represent with the regulator for looking at it, in its context and the rightness of things.

Moderator: Thank you. As there are no further questions from the participants, I would now like to hand the conference over to the management for closing comments. Over to you, sir.

V. Suryanarayanan: Thanks, everyone, for attending the conference. The company is on a forward momentum, and we will continue to keep growing well and be profitable. Thank you.

Moderator: On behalf of DAM Capital Advisors, that concludes this conference. Thank you for joining us, and you may now disconnect your lines. Thank you.