IFS Capital Ltd

Growth Momentum Likely To Flow Into 2012

*IFS Capital Ltd ("IFS") announced its final year results on 24 February 2012. Pre-tax profit ("PBT") was up by 35.1% contributed by maiden profits from its business expansion in Malaysia and Indonesia. We see further growth with its expanded scope of operations and additional manpower. We maintain an **Invest** rating with an intrinsic value of S$0.595.*

Key Developments:

Growth to persist on in 2012: IFS has positioned itself ready for growth in 2012 by increasing its staff count and obtaining its key Malaysian money lending license in 2011. This provides IFS with various avenues for organic growth. We note that the markets in which IFS operates are expected to grow at an increased rate which will potentially assist IFS in its growth path.

Local operations turnaround in the year: Singapore financing operations, excluding ECICS, turned around from a loss of S$605,000 in 2010 to a profit of S$1.4 million in 2011 due to increased business volumes, higher fee income and lower allowances for loan losses and impairment of investments as well as a tax credit.

Thailand flooding impact was small; regulatory tax and financing costs were main contributors of profit slowdown: IFS Thailand's 4Q results showed little impact from the flooding in Thailand, with top line and EBIT growth of 8.4% and 7.5% respectively. Growth for the year was also partially supported by ongoing growth from infant revenue drivers such as their leasing and hire purchase license acquired in late 2009. However, cost pressures from increased borrowing cost and a change in corporate income tax rate affecting deferred tax adjustment from its deferred tax resulted in a 20% YoY decline in NPAT.

Higher dividends en-route: IFS has declared an increase in its dividend payout from 1.5 S cents per share in 2010 to 1.75 S cents in 2011. This reflects a 4.5% dividend yield for the year, offering decent cash payback to investors on top of capital gains upside.

Invest

- Intrinsic Value $0.595
- Prev Closing $0.385

Main Activities

IFS Capital Limited is an established financial institution involved in commercial, alternative and structured finance, private equity investments as well as credit insurance, bonds and guarantees. Besides Singapore, IFS also has operations in Malaysia, Indonesia and Thailand.

Financial Highlights

(Y/E Dec) S$m	FY11	FY12F	FY13F
Net Interest Inc	16.9	18.3	19.5
Net Earned Prem	2.8	2.9	3.0
Fee and Comm	9.6	11.0	12.7
Invt & Other Inc	2.2	2.3	2.4
Net Profit	7.7	8.0	10.2

Source: SIAS Research estimate

Key ratios (FY12F)	
Return on Equity	5.5%
Return on Asset	2.2%
Debt/Equity	1.3
Price/Earnings	7.2
Price/Book	0.4

Source: SIAS Research Estimate

Indexed Price Chart

Green (FSSTI)
White (IFS Capital)

Source: Bloomberg

52wks High-Low	*S$0.535-0.295*
Number of Shares	*150.388m*
Market Capitalization	*S$57.90 m*

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Surviving the Roller Coaster year

Result summary: IFS survived the volatile year from external events such as the Thailand flooding and the debt problems in the West with a PBT growth of 35.1% YoY. This was largely supported by strong results in the second half of the year with solid bottom line growth of 108.0% and 378.4% YoY increase in PBT for the third and fourth quarters respectively. Segmental results for the year showed growth originating from non-interest income due to improvement in financing income from increased business volumes and a significant loan repayment.

Net interest income ("NII") for the year was down by 11.6% due to lower recoveries of suspended interest from non-performing loans and repayments of various loans compared to 2010. Net earned premium revenue, its smallest revenue segment, had also declined by 18.8% YoY to S$2.8 million in 2011 due mainly to lower credit insurance business volume and lower premium rates charged.

Cost overheads mainly from business expansion: IFS has also expanded its staff force in 2011, reflecting a 7% increase in staff costs which contributed to the bulk of the increase in operating expenses. However, consistent with its 3Q results, we have seen a surge in PBT margin from 20.5% in 2010 to 28.0% in 2011, implying increased efficiency despite additional overheads.

Cause of decline in ROE lies with tax: Our modified dupont analysis indicates that the main cause of the slight decline in ROE from 5.8% to 5.4% originates from the loss in income from tax credits in 2010. We note that the change is relatively large in terms of its magnitude - this has caused a S$2.4 million difference in tax revenue (2010: tax credit of S$1.3 million vs 2011: tax expense of S$1.1 million).

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Figure 1: Group Result Summary

(S$'m)	2010	2011	Change (%)
Net interest income	19.1	16.9	-11.6%
Net earned premium revenue	3.5	2.8	-18.8%
Non-interest income	9.3	11.8	27.4%
Total income	31.9	31.5	-1.1%
Operating Expenses	(18.1)	(19.4)	7.3%
Operating Profit Net Claims & Allowances	13.8	12.1	-12.1%
Net Claims Reversal	0.2	1.3	NM
Allowances & Impairments	(7.5)	(4.6)	-38.2%
Profit before tax	6.5	8.8	35.1%
Tax (Expense) / Credit	1.3	(1.1)	NM
Profit after Tax	7.9	7.7	-2.1%
Attributable Profit after NCI	7.1	7.0	-2.1%

Source: Company

Figure 2: Modified Dupont Analysis

	FY10	FY11
Tax burden	1.20	0.87
PBT margin	20.5%	28.0%
Asset Turnover	0.1	0.1
Financial Leverage	2.5	2.5
Return on Equity	5.8%	5.4%

Source: Company

Regional Operations Gaining Significant Momentum

Overview: IFS's regional operations in Indonesia, Malaysia and Thailand had grown significantly with a 62.3% YoY increase in PBT due to higher business volumes across all three regions. However, regional NPAT for the period fell 15.7% due to an increase in tax paid.

Cost pressures present in Thailand segment: IFS went through the impact of the Thailand flood relatively unscathed, reflecting an 8.4% increase in total revenue (2010: 247.9 million Baht vs 2011: 268.8 million Baht). However, Thailand was affected by the Royal Decree's adoption of a reduced corporate income tax rate, which caused the company to recognize deferred tax expenses in 2011. Higher borrowing cost and provision for bad debts also contributed to a slowdown in Thailand's bottom line.

Volume growth in Indonesia and Malaysia: IFS stated that both its Indonesia and Malaysia segments have reported higher profit with increased business volumes. As mentioned in our previous report, IFS is consistent in its expansion plans with respect to its loan assets and client base in these two countries. In particular, Malaysia offers IFS increased opportunities with its acquisition of the money lending license in 2011.

Figure 3: Regional Operations Result Summary

(S$ m)	Full Year		Change
	2010	2011	(%)
Net interest Income	8.1	7.8	-3.4
Non-Interest Income	3.8	5.0	30.5
Operating Expenses	-7.2	-6.7	-7.6
Operating Profit before Allowances	4.6	6.0	31.1
Allowances	-1.2	-0.5	-59.4
Profit before tax	3.4	5.6	62.3
Income tax expenses	0.6	-2.2	NM
Profit after Tax	4.0	3.4	-15.7
Group's share of PAT based on % of shareholdings	3.2	2.6	-18.7

Source: Company

NM: Not meaningful

Value Prospects

Despite taken aback by higher tax paid in 2011, we see the overall growth in business volume as a positive sign in the company's growth. We see growth persisting in future due to increased involvement and exposure regionally outside of Singapore. Furthermore, investment activities in Indonesia, one of IFS's key markets in the region, are likely to grow with two credit rating agencies, Fitch and Moody's, upgrading Indonesia to investment grade.

IFS's Malaysia segment will still continue to provide a source of growth with its access to key government contracts. Moreover, we see further improvement from its maiden contribution in its money lending license. **Maintain: Invest**

Figure 4: Economic Profit Model

S$ m	FY11	FY12F	FY13F	FY14F
EBIT		9.65	12.29	14.43
Tax on EBIT		-1.64	-2.09	-2.45
NOPLAT (Company)		8.01	10.20	11.97
Invested Capital		333.37	329.56	367.87
% of Debt		56.4%	51.9%	52.8%
% of Equity		43.6%	48.1%	47.2%
WACC		3.8%	3.9%	3.9%
Capital Charge		12.53	12.97	14.34
Economic Profit		-4.52	-2.76	-2.37
Discount Rate		0.94	0.89	0.84
Present Value		-4.27	-2.46	-1.99
Book Value	143.7	Risk Free		2.5%
Explicit Value	-8.7	Beta		0.688
Terminal Value	-45.5	Market RP		5.00%
Value of Firm (S$ m)	89.5	Cost of Equity		5.94%
Number of Shares (m)	150.4	Cost of Debt		2.50%
Value per share (S$)	0.595	LT Growth		1.50%

Source: SIAS Research Estimates

Figure 5: Financial Forecasts and Estimates

S$ m	FY08	FY09	FY10	FY11	FY12F	FY13F	FY14F	FY15F
Net Interest Income	11.1	13.1	19.1	16.9	18.3	19.5	20.7	22.0
Net Earned Premium Revenue	3.8	5.8	3.5	2.8	2.9	3.0	3.0	3.1
Fee & Commission income	6.4	6.4	7.5	9.6	11.0	12.7	13.9	14.9
Investment & Other Income	4.9	3.7	1.8	2.2	2.3	2.4	2.4	2.5
Net Profit	8.0	6.6	7.9	7.7	8.0	10.2	12.0	11.9
Total Current Assets	262.4	248.0	230.0	272.0	227.1	225.6	266.0	266.7
Total Non-Current Assets	131.0	109.0	95.7	121.5	106.2	104.0	101.9	99.9
Total Current Liabilities	211.1	180.5	166.1	214.8	153.2	136.2	159.5	143.3
Total Non-Current Liabilities	61.4	49.1	17.7	35.1	34.8	34.8	34.8	34.8
Total Equity	121.0	127.5	141.9	143.7	145.3	158.5	173.5	188.4
Cash from Operating Activities	14.0	95.2	44.8	-71.3	9.1	11.5	13.4	13.7
Cash from Investing Activities	-6.6	-12.2	-5.2	-1.7	0.0	0.0	0.0	0.0
Cash from Financing Activities	4.6	-81.4	-32.6	69.2	-22.6	-3.0	-3.0	-23.0
Net change in cash	12.0	1.6	6.9	-3.8	-13.5	8.5	10.4	-9.3
Return on Common Equity (%)	11.3%	5.3%	5.8%	5.4%	5.5%	6.7%	7.2%	6.6%
Return on Assets (%)	1.8%	1.8%	2.3%	2.1%	2.2%	3.1%	3.4%	3.2%
Debt/Equity	2.3	1.8	1.3	1.7	1.3	1.1	1.1	0.9
Current Ratio	1.2	1.4	1.4	1.3	1.5	1.7	1.7	1.9
EPS (S cents)	5.9	4.3	4.7	4.6	5.3	6.8	8.0	7.9
BV/Share (S cents)	80.4	84.8	94.3	95.5	96.6	105.4	115.4	125.3
P/E Ratio	6.5	9.0	8.2	8.4	7.2	5.7	4.8	4.9
P/B Ratio	0.5	0.5	0.4	0.4	0.4	0.4	0.3	0.3

Source: SIAS Research estimates

Rating Definition:

Increase Exposure – The current price of the stock is significantly lower than the underlying fundamental value higher level. Readers can consider increasing their exposure in their portfolio to a higher level.

Invest – The current price of the stock is sufficiently lower than the underlying fundamental value of the firm. Readers can consider adding this stock to their portfolio.

Fairly Valued – The current price of the stock is reflective of the underlying fundamental value of the firm. Readers may not need to take actions at current price.

Take Profit – The current price of the stock is sufficiently higher than the underlying fundamental value of the firm. Readers can consider rebalancing their portfolio to take advantage of the profits.

Reduce Exposure - The current price of the stock is significantly higher than the underlying fundamental value of the firm. Readers can consider reducing their holdings in their portfolio.