

## IFS Capital Ltd

### Maintaining Strong Growth Momentum

IFS Capital Ltd's (IFS) 2Q 2012 income before operating expenses and net attributable profit rose by 21.8% and 37.6% respectively over 1Q 2012, led by higher net earned premium and non-interest income. Loans and related receivables rose by 3.9% quarter-on-quarter. However, net interest income fell by 2.7% quarter-on-quarter, reflecting lower net interest margin in 2Q 2012.

We are of the view that the decline is due to the maturity of certain high yielding loans and that net interest income should continue to grow quarterly on the back of sustained volume growth in 2H 2012. **Maintain Invest.**

#### Key Developments:

**Net Interest Income Strength Reflected in Year-on-Year Growth:** Net interest income had actually grown by 15.4% year-on-year in 2Q 2012, on loans and related receivables growth of 32.5%, and reflected well on the company's performance over the last 12 months. 2Q 2012 income before operating expenses grew by a reasonable 5.9% as net earned premium and non-interest income fell marginally by S\$114k year-on-year.

**Higher Costs Lowered Year-on-Year Growth:** Year-on-year growth for pre-tax profit was dragged lower by higher operating costs. Pre-tax profit grew by 1.1% in 2Q 2012. As IFS enjoyed a tax credit of S\$126k in 2Q 2011 versus an expense of S\$740k in 2Q 2012, net profit was 32.4% (S\$929k) lower than a year ago.

**2H Outlook Remains Positive:** We remain optimistic of net interest income on the back of sustained volume growth. The company had also guided higher premium income in 2H 2012. On the whole, the 2Q numbers suggest healthy operations and that continued revenue growth should help to offset operating cost increments over the last 12 months. IFS's 2H 2011 tax expense was S\$1.04m versus only S\$0.091m in 1H 2011. 1H 2012 tax expense was S\$1.4m. Therefore, IFS should report healthier year-on-year after-tax profit growth rates in 2H 2012.

## Invest

- Intrinsic Value S\$0.560
- Prev Close S\$0.375

#### 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	18.9	21.0
Net Earned Prem	2.8	2.4	2.5
Fee and Comm	9.6	10.8	12.4
Invst & Other Inc	2.2	3.2	3.8
Net Profit	7.7	8.3	8.9
EPS (S cents)	4.6	5.1	5.4

Source: Company, SIAS Research

#### Key ratios (FY12F)

PER	7.4
P/BV	0.41
Return on Common Equity	5.5%
Return on Assets	2.0%
Gross Debt to Common Equity	180.1%
Current ratio	1.3

Source: SIAS Research

#### Indexed Price Chart

Green (FSSTI)  
White (FC)



Source: Bloomberg

52wks High-Low	S\$0.445 /S\$0.295
Number of Shares	150.39m
Market Capitalization	S\$56.4m

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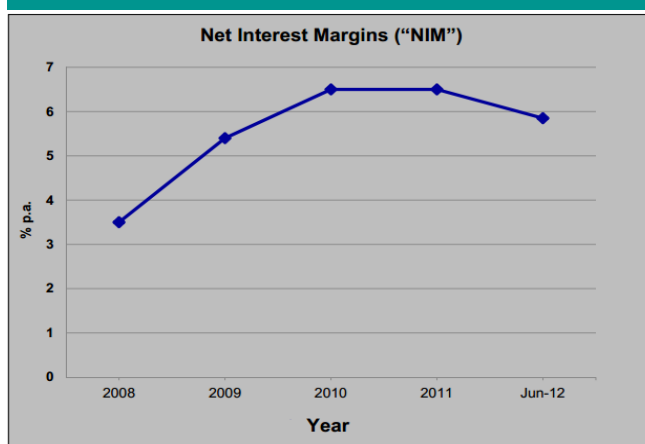
## Results Analysis and Outlook

**Non-Interest Income:** Non-interest income in 2Q 2012 was S\$4.13m versus S\$4.19m in 2Q 2011. Fee and commission income was S\$2.68m while investment income was S\$1.42m. IFS earned a one-off fee income of S\$1.4m recognized in Jun 2011 upon settlement of a property loan. Excluding this item, fee and commission income had actually rose by 15% year-on-year in 2Q 2012. The 44.6% quarterly increase in fee income actually reflected higher business volume that resulted in higher factoring and loan fees.

The absence of the one-off S\$1.4m fee income in 2Q 2012 was fortunately offset by higher investment income (+S\$0.97m over 1Q 2012). We expect investment income to be about S\$2.75m for the whole of FY12F. On the whole, we forecast IFS to make S\$13.9m of non-interest income in 2012.

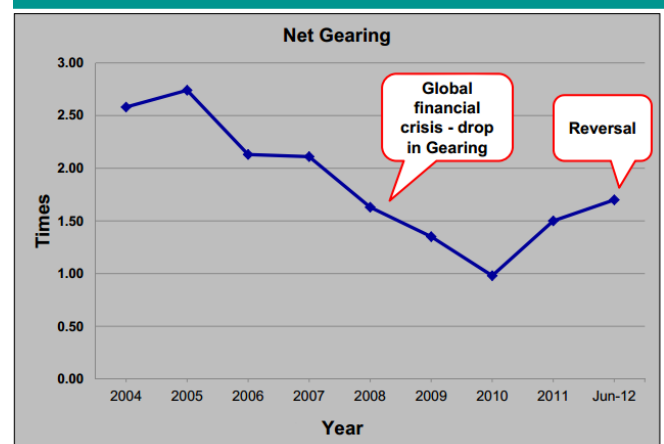
**Interest Income:** Net interest income rose year-on-year, but fell quarter-on-quarter. We do not view this observation as a decline in growth as volume continued to expand. The company experienced rising net interest margin since 2007 as it had tightened credit and charged higher interest rates during and after the US Financial Crisis. By the end of 2011, credit conditions have reversed somewhat with the company adding volume and charging lower interest rates for the same loan. Conditions have yet to fully normalize as lenders have remained cautious due to the ongoing Eurozone debt crisis. Higher volume is reflected by the group's rising gearing, which implies higher lending. We are encouraged by the management's remarks that new customers contributed a larger proportion of the increase in volume. On the whole, higher volume should over time offset lower interest margin. In the interim, expansion in higher yielding regimes such as Indonesia should continue to offset margin pressure.

Figure 1: Net Interest Margin Came Down



Source: Company

Figure 2: Gearing Went Up → Higher Volume



Source: Company

Gearing in Figure 2 is defined as debt net of cash held in IFS excluding ECICS.

**Forecasts and Valuation:** Our impression of the 2Q results is that growth has been obscured by higher costs and that the results could have been more stellar given more aggressive loan practices. Nonetheless, global financial and economic conditions remain volatile with on-going uncertainty over debt and fiscal imbalances in the US and Europe. Therefore, the company's prudence is not unjustified. That said, underlying volume expansion and 1H growth achieved suggests that IFS will still be able to deliver full year growth at both the top-line and bottom-line.

We revised our forecasts to factor in higher full year revenue potential, as well as higher operating costs faced in 1H 2012. Total income for FY12F is now expected to be S\$35.2m (versus S\$34.5m previously). Forecast net profit after minority interest is revised moderately to S\$7.6m (previously S\$8.0m). The net impact on valuation is not substantial with an updated intrinsic value of S\$0.560 (previously S\$0.595). **Maintain Invest.**

**Figure 1: Results Analysis**

	2Q 2012	1Q 2012	4Q 2011	2Q 2011	1Q 2011	QoQ	YoY
Net interest income	4.79	4.92	4.85	4.15	3.18	-2.7%	15.4%
Net earned premium revenue	0.55	0.42	0.94	0.60	0.56	29.1%	-8.9%
Non-interest income	4.13	2.43	2.98	4.19	2.63	70.1%	-1.5%
Total income	9.46	7.77	8.77	8.94	6.37	21.8%	5.9%
Operating expenses	-5.47	-5.21	-5.19	-5.09	-4.43	4.9%	7.4%
Operating profit net claims and allowances	4.00	2.56	3.58	3.85	1.94	56.2%	3.9%
Net claims reversal	-0.14	-0.04	1.35	-0.01	0.07	288.6%	NM
Allowances & impairment	-0.90	-0.13	-2.30	-0.91	-0.55	615.1%	-1.1%
Profit before tax	2.96	2.40	2.63	2.93	1.46	23.4%	1.1%
Tax	-0.74	-0.69	-0.50	0.13	-0.22	6.6%	NM
Profit after tax	2.22	1.70	2.14	3.05	1.24	30.2%	-27.3%
Attributable profit	1.93	1.41	2.03	2.86	1.00	37.6%	-32.4%
<b>Non Interest Income</b>							
Fee & commission	2.68	1.85	2.25	3.74	1.86	44.6%	-28.3%
Investment income	1.42	0.45	0.35	0.33	0.67	216.8%	325.2%
Other income	0.03	0.13	0.39	0.12	0.10	-74.0%	-72.5%
<b>Selected Balance Sheet Items</b>							
Total Receivables (1)	303.6	292.1	277.2	229.2	203.7	3.9%	32.5%
Other Investments	55.7	53.3	52.7	40.0	46.7	4.4%	39.3%
Cash	29.7	32.5	29.7	44.2	44.8	-8.6%	-32.8%
Total Borrowings	243.6	232.6	215.4	174.1	154.4	4.7%	39.9%
Total Common Equity	133.6	135.4	134.6	131.8	132.9		
<b>Gross Gearing (2)</b>	<b>1.71</b>	<b>1.61</b>	<b>1.50</b>	<b>1.24</b>	<b>1.09</b>		
<b>Ann. Return on Avg. Com. Equity</b>	<b>5.8%</b>	<b>4.2%</b>	<b>6.0%</b>	<b>8.7%</b>	<b>3.0%</b>		
	<b>1H 2012</b>	<b>1Q 2012</b>	<b>2011</b>				
<b>Net Interest Margin</b>	5.9%	5.9%	6.5%				

(1) Total receivables refer to loans, advances, hire purchase and leasing receivables (non-current assets) and trade and other receivables (current assets). (2) Net Gearing = Total Borrowings / Total Equity Source: Company, SIAS Research

**Figure 2: Valuation**

S\$m	FY12F	FY13F	FY14F
Profit Before Tax and Interest Expense	16.5	18.3	20.5
Tax on EBIT	-2.1	-2.3	-2.6
NOPLAT	14.4	16.0	17.9
Invested Capital	359.0	399.5	442.7
% of Debt	60.0%	62.7%	65.1%
% of Equity	40.0%	37.3%	34.9%
WACC (%)	4.6%	4.4%	4.3%
Capital Charge	16.4	17.7	19.0
Economic Profit	-2.0	-1.7	-1.1
Terminal Value			-51.0
Discount Factor	0.98	0.94	0.90
Present Value	-1.9	-1.6	-1.0
Book Value	134.6	Risk Free Rate	2.50%
Explicit Value	-4.5	Beta	0.70
Terminal Value	-45.9	Market RP	7.50%
Value of Equity	84.1	Cost of Equity	7.77%
Number of Shares (m)	150.4	Cost of Debt	2.8%
Value per share (S\$)	0.560	LT Growth	2%

Source: SIAS Research

**Figure 3: Financial Forecasts and Estimates**

	FY09	FY10	FY11	FY12F	FY13F	FY14F
Net Interest Income	13.1	19.1	16.9	18.9	21.0	22.4
Net Earned Premium Revenue	5.8	3.5	2.8	2.4	2.5	2.5
Fee & Commission Income	6.4	7.5	9.6	10.8	12.4	14.2
Investment & Other Income	3.7	1.8	2.2	3.2	3.8	4.4
Net Profit After Tax	6.6	7.9	7.7	8.3	8.9	9.7
PATMI	6.5	7.1	7.0	7.6	8.1	8.8
Total Current Assets	248.0	230.0	272.0	311.7	343.4	382.2
Total Non-Current Assets	109.0	95.7	121.5	122.8	134.8	150.1
Total Current Liabilities	180.5	166.1	214.8	247.2	279.7	320.7
Total Non-Current Liabilities	49.1	17.7	35.1	38.4	44.0	51.1
Total Equity	127.5	141.9	143.7	149.0	154.5	160.5
Cash from Operating Activities	95.2	44.8	-71.3	-38.7	-37.7	-33.9
Cash from Investing Activities	-12.2	-5.2	-1.7	-3.4	-6.1	-11.1
Cash from Financing Activities	-81.4	-32.6	69.2	32.2	34.2	43.7
Net Change in Cash	1.6	6.9	-3.8	-9.9	-9.6	-1.3
Return on Common Equity	5.3%	5.5%	5.2%	5.5%	5.7%	6.0%
Return on Assets	1.8%	2.3%	2.1%	2.0%	2.0%	1.9%
Gross Debt / Common Equity	143.1%	110.0%	160.1%	180.1%	200.3%	225.3%
Current Ratio	1.4	1.4	1.3	1.3	1.2	1.2
EPS (S cents)	4.34	4.72	4.63	5.05	5.40	5.87
BV / Share (S cents)	93.0	88.2	89.5	92.5	95.7	99.0
P/E Ratio	8.64	7.94	8.10	7.43	6.94	6.39
P/B Ratio	0.40	0.43	0.42	0.41	0.39	0.38

Casting errors may occur due to the effects of rounding.

Source: Company, SIAS Research

**Rating Definition:**

**Increase Exposure** – The current price of the stock is significantly lower than the underlying fundamental value. 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.

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