IFS Capital Ltd

40% Growth in Bottom-Line

IFS Capital Ltd (IFS) announced a strong set of 1Q results with net interest income rising by 54.8% year-on-year to S$4.9m. Net attributable profit rose by 40% year-on-year to S$1.4m in 1Q 2012. We expect further loan volume growth in Malaysia, Thailand and Indonesia to deliver growth, particularly in 1H 2012. ***Maintain Invest.***

Key Developments:

Full Recovery at Thailand Subsidiary: Following a challenging November, IFS experienced a strong recovery in business volume at its Thailand business, leading to the subsidiary delivering record profitability in 1Q FY12. Accordingly, both Indonesia and Malaysia also delivered strong profit and volume growth, said to be in excess of double digits. Singapore remained a competitive market, but it still delivered strong profit growth of 16% year-on-year in 1Q FY12 (S$403k).

Gross Written Premium Grew 7.5%: The growth in gross premium suggested expansion in the underlying insurance business volume. However, higher gross provision for unexpired risks led to a 24.6% decline in net earned premium revenue. Part of the provisions made in 1Q will be gradually written back due to the technical actuarial provisioning process – average profitability is actually higher. However, reversals may be offset by incremental provision from new business volume.

Growth Plans Lined-Up: IFS expects higher demand in Malaysia in 2012 – 2013 on the back of certain infrastructure projects in KL. Over in Indonesia, IFS is looking at extending to major cities beyond Jakarta to better reach out to prospects in other commercial centers. The focus will still be on corporates at the moment. The Thai market may present more new product opportunities when liberalized.

We are encouraged by the strong set of results delivered in 1Q 2012. Our view is that such momentum should continue into 2Q 2012. We largely maintain our forecasts and valuation on IFS as we await further outlook visibility into 2H 2012. However, its growth plans suggest that the company's longer term outlook remains healthy.

Invest

- Intrinsic Value S$0.595
- Prev Close S$0.390

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	8.9	9.6
EPS (S cents)	4.6	5.3	5.8

Source: Company, SIAS Research

Key ratios (FY12F)	
PER	7.33
P/BV	0.42
Return on Common Equity	5.8%
Return on Assets	2.2%
Gross Debt to Common Equity	167.6%
Current ratio	1.3

Source: SIAS Research

Indexed Price Chart

Green (FSSTI)
White (IFS)

Source: Bloomberg

52wks High-Low	*S$0.480 /S$0.295*
Number of Shares	*150.39m*
Market Capitalization	*S$58.65m*

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Results Analysis and Outlook

Interest Income: Net interest income rose by 1.5% quarter-on-quarter and 54.8% year-on-year to S$4.92m. Net interest income was S$4.85m in 4Q 2011 and S$3.18m in 1Q 2011. The increase was largely driven by volume growth as evidenced by a 5.4% quarter-on-quarter and 43.4% year-on-year increase in total receivables – Loans, advances, hire purchase and leasing receivables plus trade and other receivables on the balance sheet.

Net interest income would have been higher if not for a decline in net interest margin from 2011 (6.5%) to 1Q 2012 (5.9%). The decline was due to the maturity of certain high yielding loans and higher loan volume. We have the impression that IFS has been less selective about the yield of new loans to build a larger business base in its target markets.

Nonetheless, the company remarked that it is looking towards replacing some of the higher yielding loans in its portfolio to maintain its net interest margin and expanding in Indonesia - a higher margin market.

ECICS Limited: ECICS reported 6.1% higher gross written premium from S$1.955m in 1Q 2011 to S$2.075m in 1Q 2012. These are unconsolidated figures. However, a broad based increase in costs in areas such as higher unexpired risks provisioning, higher operating expenses, lower reversal of insurance receivables led this unit to report S$0.181m of net profit after tax versus S$0.674m in 1Q 2011.

The insurance business may benefit from continued demand for bond and guarantees given the ongoing stream of infrastructural and housing projects. The company also expects customers to be “more receptive” to credit insurance against export receivables due to the heightened credit risk in the Eurozone.

Gross provision for unexpired risks was particularly high in 1Q FY12, at 31.7% of gross written premiums or S$651k. Gross provision for unexpired risks was only 3.2% of gross written premiums in the whole of 2011.

The company explained that the higher than normal provision was due to more new business for bonds and guarantees. For each new business underwritten, the provision is higher at the onset before reversals are gradually made, leading to lower initial profitability. In subsequent quarters, whether gross provision will decline will depend on the ratio of new to recurring premiums.

Although ECICS made S$0.181m in 1Q FY12, we think that ECICS would also have reported profit growth had the provision been only 3.2% of gross premiums,

Figure 1: Results Analysis

Income Statement Items	**1Q 2012**	**4Q 2011**	**1Q 2011**	**QoQ**	**YoY**
Net interest income	4.92	4.85	3.18	1.5%	54.8%
Net earned premium revenue	0.42	0.94	0.56	-55.2%	-24.6%
Non-interest income	2.43	2.98	2.63	-18.5%	-7.8%
Total income	7.77	8.77	6.37	-11.4%	21.9%
Operating expenses	-5.21	-5.19	-4.43	0.5%	17.6%
Operating profit before net claims and allowances	2.56	3.58	1.94	-28.6%	31.8%
Net claims (incurred) / reversal	-0.04	1.35	0.07	-102.6%	NM
Allowances & impairment	-0.13	-2.30	-0.55	-94.5%	-77.3%
Profit before tax	2.40	2.63	1.46	-8.9%	64.7%
Tax	-0.69	-0.50	-0.22	40.2%	219.8%
Profit after tax	1.70	2.14	1.24	-20.2%	37.5%
Attributable profit	**1.41**	**2.03**	**1.00**	**-30.6%**	**40.0%**
Non-Interest Income					
Fee & commission	1.85	2.25	1.86	-17.5%	-0.6%
Investment income	0.45	0.35	0.67	29.2%	-33.7%
Other income	0.13	0.39	0.10	-67.0%	33.7%
Selected Balance Sheet Items					
Total receivables (1)	292.1	277.2	203.7	5.4%	43.4%
Other investments	53.3	52.7	46.7	1.1%	14.3%
Cash	32.5	29.7	44.8	9.7%	-27.4%
Total borrowings	232.6	215.4	154.4	8.0%	50.7%
Total common equity	135.4	134.6	132.9		
Gearing	**1.59**	**1.5**	**0.99**		
Ann. Return on Avg. Com. Equity	**4.2%**	**6.0%**	**3.0%**		
	1Q 2012	**2011**			
Net Interest Margin	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).

Source: Company, SIAS Research

Outlook: We like IFS's focus on expanding the financing business and the growth that it has achieved in the execution of this strategy. Across Malaysia, Indonesia and Thailand, there are untapped niches that IFS can work on, such as continuing to monetize its money lending license in Malaysia, geographical expansion in Indonesia and new market segments in Thailand.

In view of these circumstances as discussed above, our forecasts for IFS are somewhat reasonable. However, investment and other income may decline slightly as IFS has sold off its equity positions in 3Q 2011. Accordingly, we also maintain our rating and valuation on IFS.

We see two key risks against the company – a) how fast ECICS will reverse some its provisions and b) the risk of further loan impairments and allowances as IFS raises its lending base. The company made lower allowances for loan losses in 1Q 2012. In addition, persistently high provision for ECICS in the future, if observed, may imply more cautious risk appetite by the company in certain sectors.

Figure 2: Valuation

S$m	FY12F	FY13F	FY14F
Profit Before Tax and Interest Expense	16.9	18.4	19.8
Tax on EBIT	-2.2	-2.4	-2.5
NOPLAT	14.7	16.1	17.3
Invested Capital	359.0	384.4	414.5
% of Debt	60.0%	61.0%	62.2%
% of Equity	40.0%	39.0%	37.8%
WACC (%)	4.6%	4.5%	4.4%
Capital Charge	16.4	17.3	18.4
Economic Profit	-1.7	-1.3	-1.1
Terminal Value			-47.3
Discount Factor	0.96	0.92	0.88
Present Value	-1.6	-1.2	-1.0
Book Value	134.6	Risk Free Rate	2.50%
Explicit Value	-3.8	Beta	0.70
Terminal Value	-41.6	Market RP	7.50%
Value of Equity	89.2	Cost of Equity	7.77%
Number of Shares (m)	150.4	Cost of Debt	2.8%
Value per share (S$)	0.595	LT Growth	2%

Source: SIAS Research

Figure 3: Financial Forecasts and Estimates

S$m	FY09	FY10	FY11	FY12F	FY13F	FY14F
Net Interest Income	13.1	19.1	16.9	18.3	19.5	20.0
Net Earned Premium Revenue	5.8	3.5	2.8	2.9	3.0	3.2
Fee & Commission Income	6.4	7.5	9.6	11.0	12.7	14.6
Investment & Other Income	3.7	1.8	2.2	2.3	2.4	2.5
Net Profit After Tax	6.6	7.9	7.7	8.9	9.6	10.2
PATMI	6.5	7.1	7.0	8.0	8.7	9.2
Total Current Assets	248.0	230.0	272.0	302.2	327.7	354.2
Total Non-Current Assets	109.0	95.7	121.5	117.2	122.4	129.1
Total Current Liabilities	180.5	166.1	214.8	233.6	254.1	276.6
Total Non-Current Liabilities	49.1	17.7	35.1	36.0	39.5	43.4
Total Equity	127.5	141.9	143.7	149.9	156.5	163.3
Cash from Operating Activities	95.2	44.8	-71.3	-16.6	-18.6	-22.0
Cash from Investing Activities	-12.2	-5.2	-1.7	-1.1	-1.1	-1.1
Cash from Financing Activities	-81.4	-32.6	69.2	16.5	20.4	22.4
Net Change in Cash	1.6	6.9	-3.8	-1.1	0.8	-0.7
Return on Common Equity	5.3%	5.5%	5.2%	5.8%	6.1%	6.2%
Return on Assets	1.8%	2.3%	2.1%	2.2%	2.2%	2.2%
Gross Debt / Common Equity	143.1%	110.0%	160.1%	167.6%	177.2%	187.4%
Current Ratio	1.4	1.4	1.3	1.3	1.3	1.3
EPS (S cents)	4.34	4.72	4.63	5.32	5.77	6.13
BV / Share (S cents)	93.0	88.2	89.5	93.0	96.8	100.7
P/E Ratio	8.99	8.26	8.42	7.33	6.75	6.36
P/B Ratio	0.42	0.44	0.44	0.42	0.40	0.39

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.