IFS Capital Ltd

Stakes Increased in Top Performers

IFS Capital Ltd ("IFS") announced its 1QFY11 results on 13 May 2011. Income before operating expenses and net profit after tax was at S$6.4m and S$1.2m respectively – an 18.8% and 14.0% decline YoY due to a slower start in its Singapore operations for the quarter. The decrease in income is mainly due to lower recovery of suspended interest.

*IFS had also recently subscribed for additional share capital in its Indonesian subsidiary and Malaysian subsidiary. With a larger capital base for its regional operations, it is in a better position to organically grow through larger market share. We maintain our intrinsic value at S$0.640 representing a 40.7% price-value gap from the last closing price of S$0.455 and an **Invest** rating due to uncertainties in the market outlook.*

Key Developments:

Regional operations outperforming: 1QFY11 results of its regional operations showed net profit grew by 36.7% YoY – from S$0.7m to S$0.9m. This was mainly attributed to higher loans and factoring service fees from higher business volumes. Activities around the region through government fiscal policies will continue to support growth in this segment.

Singapore operations bringing overall performance down: IFS Singapore had a slow start in operations for the first quarter. However, IFS had given guidance that business volume picked up at the end of 1QFY11.

Further opportunities for growth: Leverage and gearing improved YoY, sitting at 1.3 and 1.2 times from 1.8 and 1.5 respectively. This better equips the company to pick up opportunities as they arise. Management had also given guidance on its growth by looking for opportunities regionally and in Australia.

Invest

- Intrinsic Value $0.640
- Prev Closing $0.455

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	FY09	FY10	FY11F
Net Interest Inc	13.1	19.1	22.6
Net Earned Prem	5.8	3.5	4.0
Fee and Comm	6.4	7.5	9.3
Invt & Other Inc	3.7	1.8	2.1
Net Profit	6.6	7.9	10.4

Source: SIAS Research estimate

Key ratios (FY11F)

Return on Equity	7.2%
Return on Asset	2.8%
Debt/Equity	1.8
Price/Earnings	6.9
Price/Book	99.7

Source: SIAS Research Estimate

Indexed Price Chart

Green (FSSTI)
White (IFS Capital)

Source: Bloomberg

52wks High-Low	*S$0.545-0.450*
Number of Shares	*150.388m*
Market Capitalization	*S$68.43m*

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Regional Operations Winging the Scene

IFS's regional operations continued to show strong performance, with a 36.7% YoY growth in its bottom line for the quarter due to higher growth in non-interest income. Improvement in fees was attributed to higher fees and commission income from higher business volume. Growth was partially offset by higher operating expenses for the period.

Figure 1: Regional Operations Results Summary

(S$ m)	Results		Growth
	1QFY10	1QFY11	YoY
Net Interest Income	2.0	1.8	-7.5%
Non-Interest Income	0.9	1.1	25.4%
Operating Expenses	-1.4	-1.6	9.4%
Operating Profit before Allowances	1.4	1.3	-4.6%
Allowances	-0.2	-0.1	-53.0%
Profit before Income Tax	1.2	1.2	5.9%
Income Tax	-0.5	-0.3	-41.5%
Profit after Income Tax	0.7	0.9	36.7%
Net attributable profit	0.7	0.7	5.7%

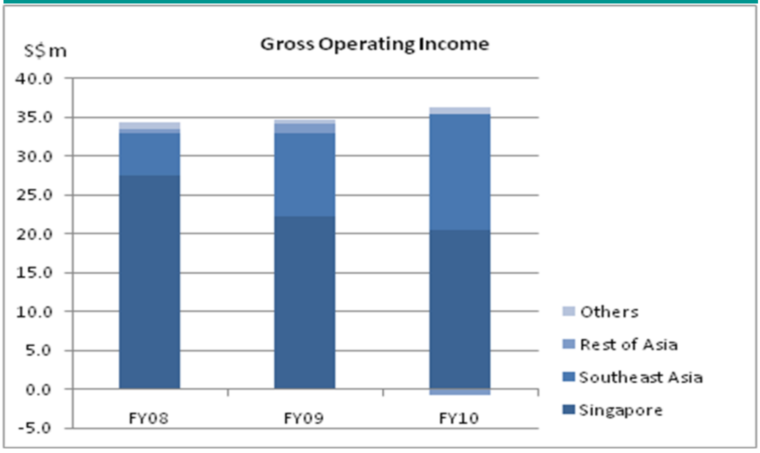
Source: Company, SIAS Research

Stronger capital base to expand its overseas operation

Back in mid-March 2011, IFS increased its Indonesia and Malaysia subsidiaries' capital base by IDR 70 billion (S$10.1m) and MYR 5 million (S$2.1m) respectively. This was executed via ordinary share issue and preference share issue through its Indonesia and Malaysia subsidiaries respectively. IFS maintained its effective interest in its Indonesian subsidiary of 85% through proportionate take-up of its shares (595,000 out of 700,000).

Our analysis indicates that the main drivers of growth are attributed to its regional operations outside of Singapore (Indonesia, Malaysia and Thailand) as shown in our previous report dated in 1st March 2011 due to higher growth in the region. This growth will be maintained through government and private sector initiatives.

Figure 2: Group Geographic Segments Overview



Source: SIAS Research, Company

Indonesia

The Indonesian Master Plan 2011 outlines the country's roadmap to the path of prosperity in the coming years, while aiming to be one of the world's top 10 economies by 2030. Hatta Rajasa, Coordinating Minister, stated that they would need IDR 932 billion (S$134.7m) in investment by 2030 to realize the plan with heavy reliance on private sector investment. The Industry Minister, MS Hidayat, stated that the Indonesian government will attempt to attract investments through regulation reforms to reduce investing costs by market participants.

Malaysia

Malaysia Prime Minister Najib Razak unveiled the Second Capital Market Master Plan (CMP2) during April 2011, a strategy aimed at improving Malaysia's capital markets. According to Najib Razak, the government forecast that capital market sizes will more than double to 4.5 trillion ringgit (S$1.85 trillion) by 2020. Similar to its Indonesian subsidiary, better capital fund flow will attract more business volume for IFS's regional operations.

With a larger capital base from their recent financing activities, both the Indonesian and Malaysian subsidiaries will be in a better position to grow IFS' overseas arm as compared to its overseas competitors.

Thailand

Thailand's 2011/12 budget plan projects a budget spending of 2.25 trillion baht, up from the current spending budget of 2.07 trillion baht which is expected to end on 30 September 2011 and will further stimulate economic activity.

Overall, increased fiscal spending in Thailand will stimulate economic activity which will in turn boost IFS' regional operations growth in the future. This will also correspondingly increase foreign currency gains due to increased economic activity and thus achieve a higher comprehensive income.

Using 1 IDR = 0.000144155777 SGD.
Source: Google Finance

Performance Review

IFS recorded a net profit for the period at S$1.2m, a 14% drop YoY. The drop in profit is due to its Singapore operations experiencing a slow start for the quarter as well as having S$2.3 million one-off recovery of interest repayment of a significant property loan last year. Moving forward, the company will recognize higher QoQ profit due to increased business volume after the end of 1QFY11.

International Enterprise Singapore (IES) had increased its turnover eligibility criteria for its trade credit insurance education program, Trade Credit Insurance Scheme (TCIS), from S$80m to S$100m. This will also contribute to increasing business volume for its trade credit insurance segment.

We also note that comprehensive income for the quarter fell to S$0.19m from S$3.2m YoY due to a large foreign currency translation difference loss mainly from the depreciation of the Thai Baht.

Figure 3: Group Result Summary

(S$ m)	**Results**		**Growth**
	1QFY10	**1QFY11**	**YoY**
Net Interest Income	5.6	3.2	-43.2%
Net Earned Premium Revenue	0.7	0.5	-26.5%
Non-Interest Income	1.5	2.6	76.8%
Total Income	7.8	6.3	-18.8
Operating Expenses	-4.1	-4.4	7.1%
Operating Profit before Net Claims and Allowances	3.7	1.9	-47.7%
Net Claims Reversal/ (Incurred) and Allowances	-1.5	-0.5	-60.6%
Profit before Income Tax	2.2	1.4	-35.8%
Income Tax Expense	-0.8	-0.2	-73.8%
Profit after Income Tax	1.4	1.2	-14.0%

Source: Company

Risks

Lower credit yield due to high liquidity: Increased global liquidity may indirectly affect loan yield achievable from the reconstruction of Japan following the earthquake and potential quantitative easing in Europe. This may potentially affect top line margins of IFS's business due to lower demand for liquidity. However, as Singapore, Malaysia, Thailand and Indonesia are all net export countries, the negative impact will be reduced with increased economic activities as a result of increased liquidity.

Potential impact of inflation cooling measures: There may be increased government policies to rein in inflation to a reasonable level through either soaking up liquidity by increasing interest rates or regulatory policies to curb policies. Lower economic activity will result if the governments lower interest rates which will affect business volumes.

Value prospects

From IFS's presentation, NPAT's decline of 14% from S$1.4m in 1QFY10 to S$1.2m in 1QFY11 was mainly attributable to an exceptional recovery of interest from repayment of a significant property loan in 1QFY10. By excluding this recovery, net interest income for 1QFY11 will only have a slight decrease YoY of only 3.7%. A brief Dupont analysis also indicated that the drop in profit is largely due to its tax burden but is partially mitigated by higher leverage ratio.

Figure 4: IFS Dupont Analysis

Period	Tax burden	Return on sales	Asset Turnover	Leverage Ratio	Return on Equity
FY10	0.9	22.8%	0.1	2.3	3.5%
1QFY11^	1.2	20.5%	0.1	2.5	5.8%

^ Quarterly figures have been annualized for comparison

Source: SIAS Research

We are optimistic on IFS due to the following reasons:

1) Profit is expected to increase from its Singapore operations with business volume picking up after the end of 1QFY11.
2) Increased stake in regional operations will spur growth in business volume through large fiscal policies by respective governments.
3) Healthy debt ratios allow IFS to pursue further opportunities around the region.

Maintain: **Invest**

Figure 5: Economic Profit Model

	FY11F	FY12F	FY13F
EBIT	13.0	16.3	17.0
Tax on EBIT	-2.6	-3.3	-3.4
NOPLAT	10.4	13.0	13.6
Invested Capital	425.4	444.9	464.9
% of Debt	69.3%	64.3%	56.4%
% of Equity	30.7%	35.7%	43.6%
WACC	4.5%	4.8%	5.2%
Capital Charge	19.3	21.3	24.2
Economic Profit	-8.9	-8.3	-10.6
Discount Rate	0.96	0.95	0.95
PV of Economic Profit	-8.5	-7.9	-10.1
Book value	141.9	Risk Free	3.0%
Explicit Value	-26.5	Beta	0.7
Terminal Value	-18.8	Market RP	7.5%
Value of Firm	96.6	Cost of Equity	8.2%
Number of Shares (m)	150.4	Cost of Debt	3.5%
Value per share (S cents)	64.0	LT Growth	1.5%

Source: SIAS Research Estimates

Figure 6: Financial Forecasts and Estimates

S$ m	FY08	FY09	FY10	FY11F	FY12F	FY13F
Net Interest Income	11.1	13.1	19.1	22.6	23.0	23.5
Net Earned Premium Revenue	3.8	5.8	3.5	4.0	4.1	4.2
Fee & Commission income	6.4	6.4	7.5	9.3	9.5	9.7
Investment & Other Income	4.9	3.7	1.8	2.1	2.2	2.2
Net Profit	8.0	6.6	7.9	10.4	13.0	13.6
Total Current Assets	262.4	248.0	230.0	332.2	351.2	370.8
Total Non-Current Assets	131.0	109.0	95.7	93.2	93.6	94.1
Total Current Liabilities	211.1	180.5	166.1	257.2	266.1	275.1
Total Non-Current Liabilities	61.4	49.1	17.7	18.2	18.8	19.3
Total Equity	121.0	127.5	141.9	149.9	160.0	170.5
Cash from Operating Activities	14.0	95.2	44.8	99.7	103.4	106.2
Cash from Investing Activities	-6.6	-12.2	-5.2	-0.4	-0.4	-0.4
Cash from Financing Activities	4.6	-81.4	-32.6	-86.9	-90.0	-92.4
Net change in cash	12.0	1.6	6.9	12.4	12.9	13.4
Return on Common Equity (%)	11.3%	5.3%	5.8%	7.2%	8.4%	8.2%
Return on Assets (%)	1.8%	1.8%	2.3%	2.8%	3.0%	3.0%
Debt/Equity	2.3	1.8	1.3	1.8	1.8	1.7
Current Ratio	1.2	1.4	1.4	1.3	1.3	1.3
EPS (S cents)	5.9	4.3	4.7	6.9	8.7	9.0
BV/Share (S cents)	80.4	84.8	94.3	99.7	106.4	113.3

Source: SIAS Research estimates

Rating Definition:

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

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.

IMPORTANT DISCLOSURE:

SIAS Research Pte Ltd received compensation for conducting this valuation research. The estimated fair value of the stock is a statement of opinion, and not statement of fact or recommendation on the stock.

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