

GICS: Financials/Specialized Finance

Business Summary: IFS Capital is a financial institution whose core activities evolve around the provision of financial services such as commercial and structured finance, private equity investments as well as credit insurance, bonds and guarantees.

Country of Incorporation: Singapore

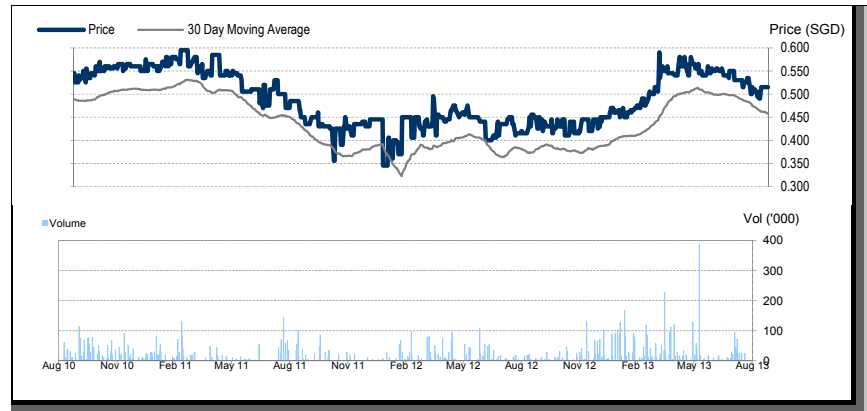
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Key Stock Statistics

52-week Share Price Range (SGD)	0.36 - 0.54
Avg Vol - 12 months ('000 shares)	18.8
Price Performance (%)	
- 1 month	-4.1
- 3 month	-7.9
- 12 month	16.3
No. of Outstanding Shares (mln)	150.4
Free Float (%)	50.8
Market Cap (SGD mln)	69.9
Enterprise Value (SGD mln)	255.6
Major Shareholders (%)	
Phillip Assets Pte Ltd	41.0
SMRT Road Holdings	6.9

Per Share Data

FY Dec.	2012	2013E	2014E
Book Value (SG cents)	92.61	92.77	95.48
Cash Flow (SG cents)	5.8	2.1	5.2
Reported Earnings (SG cents)	5.1	1.4	4.5
Dividend (SG cents)	2.0	0.5	1.8
Payout Ratio (%)	39.5	39.5	39.5
PER (x)	9.1	33.9	10.4
P/Cash Flow (x)	8.1	22.5	9.0
P/Book Value (x)	0.5	0.5	0.5
Dividend Yield (%)	4.3	1.2	3.8
ROE (%)	5.6	1.5	4.8
Net Gearing (%)	141.1	161.3	180.2

Higher provisions offset decent margin performance

- Singapore loan losses surprise negatively,** IFS's 2Q13 performance disappoints, swinging to net loss of SGD4.9 mln (vs. net profit of SGD1.9 mln for 2Q12) due to a jump in its provision for loan losses to SGD7.6 mln. The loan loss provisions include normal credit losses and default from a significant account in Singapore. While legal proceedings are underway, IFS has fully provided for this default. Meanwhile, 2Q13 operating profit fell 35.6% YoY, despite stable margins supporting net interest income growth of 15.8% YoY, as marked-to-market losses in its equity portfolio led to a 94.5% YoY drop in investment income.
- Lower earnings estimates and fair value range.** Given the jump in provision for loan losses, we cut our 2013-2014 earnings estimates by 74.2% YoY and 23.0% YoY, respectively. Meanwhile, we think non-performing loans peaked in 1H13 and expect credit costs to normalize, going ahead. However, we note that if IFS sees recoveries, there may be upside to our estimates. Following the lowering of estimates, our fair value range is reduced to SGD0.52 to SGD0.56 from SGD0.59 to SGD0.66. Our fair value continues to be derived from a weighted blend of dividend discount and peer group PBV ratios.
- Expect stronger 2H13.** We expect IFS's loan growth in Singapore to still surprise positively in 2H13 (+11.0% YoY for 1H13) and factoring volumes (+18% YoY for 1H13) to remain robust as the deleveraging by the European banks drives market share gains.
- Insurance operations expected to stabilize.** Insurance operations saw premium income growth slow to 3.1% YoY (vs. 52.9% YoY for 1Q13), as the Singapore government's property cooling measures gradually take effect and slow the bond and guarantee business. Meanwhile, higher provision for loan losses (similar significant account that impacted Singapore loan book) and claims led to an operating loss of SGD0.69 mln (vs. SGD0.36 mln profit for 1Q13). The good news is that MAS has revoked its earlier restrictions on IFS and it can now write the full range of general insurance business in Singapore.

Earnings Outlook

Revenue Drivers:

- Revenue is expected to get a boost from stronger lending activity in Singapore, while Thailand and Malaysia operations maintain a steady performance. We expect Singapore's system loan growth to be driven by market share gains as the European banks continue to de-leverage. In Indonesia, we are mindful of downside risks, because of a certain level of political uncertainty given the approach of presidential elections in 2014. We note GDP slowed to 5.8% for 2Q13 and system loan growth is now expected to come under 20%.
- While slowing domestic consumption and exports saw Thailand's system loan growth drop to 12.8% YoY (vs. 13.2% YoY for 1Q13), we expect a pick-up in lending activity for 2H13 and into 2014 as the government's infrastructure projects are rolled out. In Malaysia, government spending is expected to gather pace in 2H13 and support IFS's sub-contractor financing business. We expect fee income to grow 10% YoY for 2013-2014, supported by strong factoring volumes and insurance business ceded out.
- The insurance operations may see a slower 2H13, while longer term, we think IFS is set to reap the benefits of the MAS lifting some restrictions on its product portfolio. We expect premium income to grow 7% YoY for 2013-2014 driven by the launch of new products (contractor's all risk, work injury compensation and cargo and foreign worker medical insurance) and market share gains.

Margin Outlook:

- We expect net interest margin (NIM) to decline 14 bps and 12 bps for 2013 and 2014, as rising funding costs and competition in its international operations pressure NIM. However, we see operating costs being reined in as IFS has the flexibility to adjust performance related bonus. We forecast a steady cost-to-income ratio for 2013 and improving 30 bps in 2014.

Bottomline:

- Net profit is anticipated to decline 72.9% YoY in 2013, which means an improved performance is factored in for 2H13. We expect net profit to grow 30.3% YoY in 2H13 as impairments stabilize while loan growth remains robust. However, the risk from a turn in the interest rate cycle and the strong credit growth in IFS's markets is likely to cause credit costs to rise from their low base. We believe rising credit cost will outweigh any potential stabilization in lending margins. We forecast credit cost at 6.0% (+257.6% YoY) for 2013.
- We expect 2014 profit to rebound due to a low base and increase in net interest income and credit cost dropping to 3.0%. Main risks to our forecast include: (i) slowing growth and rising competitive pressures in Thailand and (ii) potential currency translation losses due to SGD strength vs. regional currencies, which may negatively impact book value.

Earnings Performance

FY Dec. / SGD mln	2Q13	2Q12	% Change
Reported Revenue	10.8	11.2	-3.5
Reported Operating Profit	2.5	3.9	-35.6
Depreciation & Amortization	-0.4	-0.5	-30.5
Net Interest Income / (Expense)	NA	NA	NA
Reported Pre-tax Profit	-5.1	3.0	NM
Reported Net Profit	-4.9	1.9	NM
Reported Operating Margin (%)	23.0	34.5	-
Reported Pre-tax Margin (%)	-47.4	26.4	-
Reported Net Margin (%)	-45.5	17.3	-

Source: Company data

Profit & Loss

FY Dec. / SGD mln	2011	2012	2013E	2014E
Reported Revenue	36.0	42.7	43.2	47.2
Reported Operating Profit	13.4	15.1	15.1	16.1
Depreciation & Amortization	-2.2	-2.1	-2.1	-2.1
Net Interest Income / (Expense)	NA	NA	NA	NA
Reported Pre-tax Profit	8.8	12.0	4.2	10.1
Effective Tax Rate (%)	12.8	26.4	20.0	20.0
Reported Net Profit	7.0	7.6	2.1	6.7
Reported Operating Margin (%)	37.4	35.3	34.9	34.1
Reported Pre-tax Margin (%)	24.6	28.1	9.6	21.3
Reported Net Margin (%)	19.3	17.9	4.8	14.2

Source: Company data, S&P Equity Research

Key Financial Performance

FY Dec.	2011	2012	2013E	2014E
Revenue Growth(%)	1.3	18.7	1.2	9.3
Operating Profit Growth(%)	-4.0	11.9	0.2	6.5
Net Profit Growth(%)	-2.1	9.6	-72.9	225.5
EPS Growth(%)	-2.1	10.9	-73.1	225.5
EPS 3-Year CAGR(%)	-10.4	2.0	-33.6	-0.9

Source: Company data, S&P Equity Research

Key Fundamentals

FY Dec.	2009	2010	2011	2012
ROE (%)	5.3	5.5	5.2	5.6
ROA (%)	1.9	2.4	2.0	1.9
Payout (%)	31.4	31.8	37.8	39.5

Valuation

We value IFS at SGD0.52 to SGD0.56 (down from SGD0.59 to SGD0.66) based on a weighted blend of dividend discount and PBV valuations. Our valuations factor in long term loan growth of 7.5%, with rising share of international business expected to keep net interest margin relatively stable. We have attached a target 2013 PBV of 0.8x based on a 30% discount to the median PBV of a select basket of overseas finance companies and 10% discount to the Singapore companies. The higher discount for the overseas peers largely reflects IFS's position in these markets that are relatively new to it and where it needs to build up scale.

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Page 3 of 5

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