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IFS Capital

(IFS SP/I49.SI)

Keeping up the momentum in lending to Southeast Asian SMEs

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- IFS lending business to SMEs in Southeast Asia has grown from strength to strength. 2Q19 PATMI rose to S\$3.2mn, an increase from S\$0.8mn reported in the prior year period.
- Its gross lending assets - which include factoring receivables and asset-based loans - remained stable at around S\$377mn as at end 2Q19.
- While all its lending businesses are now profitable, IFS' insurance segment still reported losses. New management at its insurance business (since January 2019) is expected to turn things around.
- We maintain our OUTPERFORM recommendation on IFS. Our fair value of S\$0.30 is based on 0.6x 2020F BVPS.

Financials & Key Operating Statistics

YE Dec SGD mn	2017	2018	2019F	2020F	2021F
Net Interest Income	19.0	20.5	24.2	26.9	28.4
PATMI	2.0	18.0	8.3	8.5	9.3
Net Profit Growth		820%	-54%	3%	9%
EPS (SGD cents)	0.5	4.8	2.2	2.3	2.5
Return on Average Equity	1.5%	11.9%	5.2%	4.9%	5.1%
Return on Average Assets	0.8%	7.8%	3.1%	2.8%	3.0%
NAV (SGD Cents)	40.5	45.0	47.2	49.5	51.9
P/B(x)	0.5	0.5	0.5	0.4	0.4
P/E(x)	41.3	4.5	9.8	9.5	8.7
Wgt. Avg. shares, diluted	376	376	376	376	376
DPS (SGD Cents)	0.3	0.6	0.4	0.5	0.5
Div Yield (%)	1.4	2.6	2.0	2.1	2.3

Source: Company Data, KGI Research

Lending business growing healthily despite headwinds; 2Q 19 results boosted by one-off item. Net interest income in 2Q19 rose 30% YoY to S\$6.2mn, which was contributed mainly by the higher business volume in its asset-based lending business. IFS grew its asset-based loan book to S\$209mn as at end 2Q19, an increase from S\$164mn as at end 2Q18. Net interest margin (NIM) improved slightly from 6.8% in 2Q18 to 6.84% in 2Q19. Meanwhile, non-interest income in 2Q19 increased 23% YoY to S\$5.9mn, due to lower reinsurance premium expenses and excess recovery by its IFS subsidiary in Thailand from their non-performing loans (NPL) accounts. We have to point out that there was a S\$2.3mn non-recurring gain arising from recovery from NPL accounts in 2Q19, which helped contribute to the 300% YoY surge in PATMI to S\$3.2mn. But even without the one-off gains, operating profits would still have increased by around 50% YoY. Given the positive trend, we expect IFS to achieve its highest annual profits since 2012 (excluding 2018 when it completed the sale of its Suntec office and reported a net gain of S\$17mn).

Figure 1: Net interest income

Net interest income (S\$'000)	2Q19	2Q18	YoY %
Factoring	3,677	3,578	2.8%
Loans, advances, hire purchases	4,596	2,974	54.5%
facility fee	-	113	(100%)
Interest income	8,273	6,665	24.1%
Interest expense	(2,035)	(1,850)	10.0%
Net interest income	6,238	4,815	29.6%

Source: Company data, KGI Research

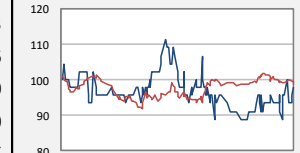
Outperform - Maintained

Price as of 23 Aug 19 (SGD)	0.22	Performance (Absolute)	
12M TP (\$)	0.30	1 Month (%)	4.8
Previous TP (\$)	0.29	3 Month (%)	7.3
Upside (%)	34.9	12 Month (%)	0.3

Trading data

Mkt Cap (\$mn)	83
Issued Shares (mn)	376
Vol - 3M Daily avg (mn)	0.0
Val - 3M Daily avg (\$mn)	0.0
Free Float (%)	39.7%

Perf. vs STI Index (Red)



Major Shareholders

Lim Hua Min	60.1%	2-Jan-19	OP S\$0.29
Dymon Asia Private Equity	6.9%	17-Oct-18	OP S\$0.29

Previous Recommendations

Insurance – new leadership. Losses in IFS insurance business segment widened to S\$5.5mn in FY2018, from a prior year loss of S\$4.7mn. On a positive note, 1H 2019 is showing indications that the restructuring effort to turn around the insurance subsidiary, ECICS Limited, is starting to bear fruits. The group has brought in industry veteran Mr Choi Kin Seng – previously COO of FWD Singapore and CEO of Etiqa Insurance Bhd, Singapore Branch – as the new CEO of ECICS Limited in January 2019.

Opportunities for consumer lending. IFS was one of only six firms selected by the Ministry of Law (MinLaw) in December 2018 to pilot a new business model for moneylending. The new moneylending model would use a more comprehensive data approach to assess a borrower. IFS Capital is well-positioned to grow in the consumer moneylending business given its track record of providing financial services to Small and Medium Enterprises (SMEs) for more than 30 years. In particular, IFS Capital could reach out to own-account worker segment, entrepreneurs and freelancers, by offering them better and faster lending decisions through the use of technology and personalised services.

Valuation & Action: We maintain our OUTPERFORM recommendation on IFS, driven by strong, stable growth in its lending business. We assign a target price of \$0.30 to IFS, based on 0.6x FY20F BVPS.

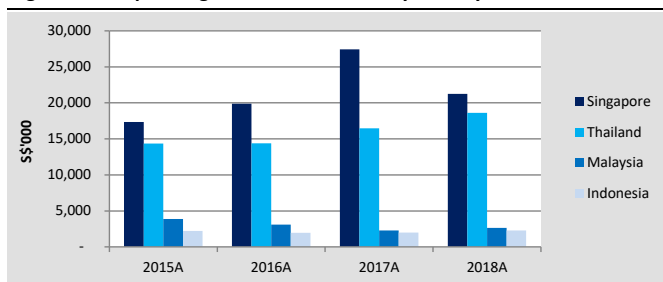
Risks: Increase in net claims from its insurance business and an economic slowdown are key risks. Meanwhile, a faster-than-expected rise in rates would impact IFS's cost of borrowings and net interest margins.

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Regional growth

ASEAN growth story. IFS derives slightly around half of its operating income from Singapore and the remainder from other countries in Southeast Asia including Thailand (42%), Malaysia (6%) and Indonesia (5%). IFS mainly provides factoring services in these countries. As such, we expect IFS's top line growth to be driven by the needs and growth plans of SMEs in the region.

Figure 2: IFS operating income breakdown by country



Source: IFS Capital, KGI Research

IFS's factoring/loan portfolios in Malaysia and Indonesia exhibit higher credit risk but the sizes of these portfolios are relatively small, as compared to the portfolios in Thailand and Singapore. The firm's operating income growth in its major markets has been stable in recent years and the company is expecting higher growth from its other markets in the near future.

Figure 3: IFS's total assets breakdown by country

Assets (\$'000)	2015	2016	2017	2018
Singapore	235,210	231,208	215,420	277,590
Thailand	140,251	154,659	175,177	186,621
Malaysia	12,099	10,620	9,747	22,794
Indonesia	5,146	8,317	10,041	18,916

Source: IFS Capital, KGI Research

SMEs are an important segment in the economies of Southeast Asia, accounting for between 30% and 60% of the countries' GDP and employing between 60% and 90% of the workforce. SMEs' definitions vary across countries but a study by Deloitte and Visa in 2015 provides a good comprehensive view across five ASEAN countries (table below).

Figure 4: Definition of SME varies among the five ASEAN countries

	Indonesia		Malaysia ¹		Philippines		Singapore		Thailand ²	
Enterprises	Turnover (USD ³ '000)	Net Assets (USD ³ '000)	Turnover (USD ³ '000)	Employee (No.)	Turnover (USD ³ '000)	Employee (No.)	Turnover (USD ³ '000)	Employee (No.)	Turnover (USD ³ '000)	Employee (No.)
Medium	200-4,000	40-800	800-6,000	30-75	340-2,300	100-199			900-6,000	16-200
Small	20-200	4-40	80-800	5-30	68-340	10-99	<74,000	<200		
Micro	<20	<4	<80	<5	<68	<10			<900	<15

Source: Deloitte. Notes: 1. Does not apply to manufacturing sector; 2. Specific figures differ across countries; 3. March 8, 2015 exchange rate used: 1 USD = 3.6 MYR, 1 USD = 44.31 PHP, 1 USD = 12646 IDR, 1 USD = 33 THB, 1 USD = 1.36 SGD

Slowing down in ASEAN but still healthy growth. Growth is expected to slow down in Southeast Asia, partly due to the trade tensions between the US and China. Forecasts by the OECD Development Centre show ASEAN's growth to slow down to 4.9% in 2019 but recover slightly to 5.0% in 2020 on healthy domestic private spending and implementation of infrastructure initiatives. Since 2015, ASEAN has worked towards regional integration in policy areas such as infrastructure and consumer protection. Furthermore, ASEAN's Economic Community (AEC) is working rapidly to reduce tariffs and improve the movements of goods and capital, which we believe would most likely benefit SMEs.

Figure 5: Selected ASEAN real GDP growth

	2017	2018	2019	Changes from the previous forecast (Nov. 2018)	2020
ASEAN-5 countries					
Indonesia	5.1	5.2	5.1	↓	5.1
Malaysia	5.7	4.7	4.4	↓	4.6
Philippines	6.7	6.2	6.0	↓	6.3
Thailand	4.0	4.1	3.5	↓	3.6
Viet Nam	6.8	7.1	6.7	-	6.6
Brunei Darussalam and Singapore					
Brunei Darussalam	1.3	0.1	1.6	↓	1.9
Singapore	3.7	3.1	2.4	↓	2.5

Source: OECD (2019), Economic Outlook for Southeast Asia, China and India 2019 - Update

Singapore's GDP growth is expected to slow down in 2019 due to weakness in manufacturing and trade-related services. The 2.4% forecast for 2019 by OECD may be too optimistic given that Singapore's Ministry of Trade and Industry's latest update in August 2019 expects growth this year to come in between 0.0% and 1.0%. On a positive note, growth may stabilise in 2020 on social and infrastructure spending, which may boost domestic demand.

Thailand's growth is forecasted to drop to 3.5% in 2019 from 4.1% in 2018, but is still an improvement from the 2.9% average between 2011 and 2015. Growth is at risk to the downside given the government's own growth forecast of 2.7-3.2% (previously 3.3%-3.8%) on the back of weak global demand and a downturn in its tourism sector. We do note a potential upside to the current bearish sentiment: the government's US\$10bn economic stimulus package to support farmers and low income groups, as well as the rate cut by the Bank of Thailand, may lend support going forward.

Indonesia is among the fastest – together with the Philippines and Vietnam - growing nations in ASEAN. GDP is expected to expand 5.1% in 2019 and 2020 as the country benefits from improvements in investment climate, better fiscal footing and resilient private consumption. Private consumption has been growing at an average of 5.1% in the past 10 years.

Malaysia is expected to slow down to 4.4% in 2019 before recovering in 2020. The government is pushing ahead with mega infrastructure projects such as the East Coast Rail Link (ECRL), Klang Valley MRT2 and LRT 3, which could lend support to growth in the medium to long term.

Moneylending in Singapore

The six firms mentioned below will be issued moneylending licenses to operate outlets in Singapore. Since a moratorium was imposed in 2012, the number of moneylending outlets declined from 215 outlets to 158 outlets currently. The six firms will be allowed to apply for licenses for up to 15 new outlets in total.

Figure 6: Six firms allowed to open new moneylending outlets

Firm	No. of outlets
Credit 21 Private Limited	4
Dey Private Limited	4
IFS Capital Limited	1
Minterest Holdings Private Limited	1
Quick Credit Private Limited	4
Xingang Investment Private Limited	1

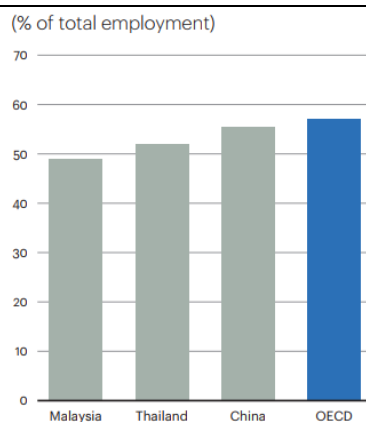
Source: Ministry of Law

Structural changes in the global economy and workforce

Two key trends that are driving structural changes in the global economy and in the labour force is the rise of technology firms and automation. Technology firms including Facebook, Alphabet (parent company of Google), Apple and Microsoft are the world’s largest companies in terms of market capitalisation but have not generated the same level of direct employment as their industrial predecessors. Meanwhile, new technologies such as Uber, Grab and Airbnb, have created platforms to allow people to earn income from the sale of their services or renting of their assets.

Automation is also expected to disrupt traditional jobs not only in manufacturing, but jobs in retail, services and well as many back-office functions. A study by the World Bank estimates that two-thirds of all jobs are susceptible to automation.

Figure 7: Employment susceptible to automation in Asian countries



Source: World Bank World Development Report, AT Kearney Analysis

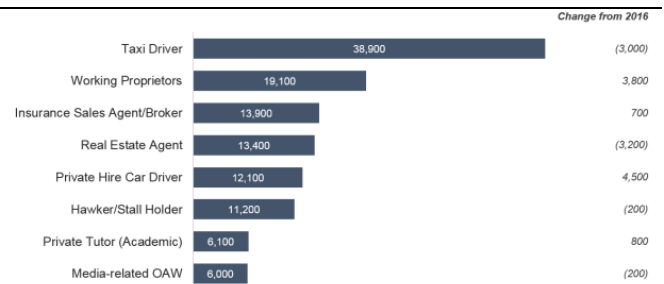
Our initial assessment IFS Capital’s potential market in the consumer segment thus looks promising given that it is riding on long-term structural trends in the workforce, as well as its 30 years of experience in financing SMEs. In Singapore, IFS Capital has indicated that it will be specifically targeting own-account workers, entrepreneurs and freelancers.

Potential market in Singapore

Own-account workers are self-employed persons who are engaged in a business without employing any paid workers.

In Singapore, the top occupations among primary own-account workers in 2017 were similar to 2016 and were in traditional jobs such as taxi drivers, working proprietors, insurance sales agents, real estate agents and newer work such as private hire car drivers.

Figure 8: Top occupations among primary own-account workers in 2017

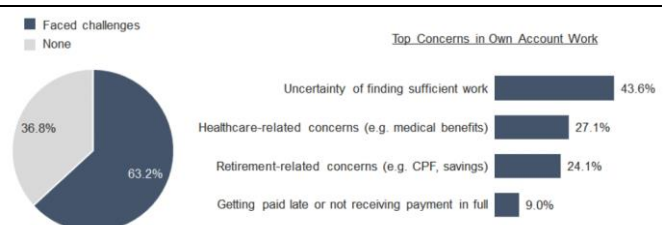


Source: Supplementary Survey on Own-Account Workers, Manpower Research & Statistics Department, MOM

Helping to finance these new workers

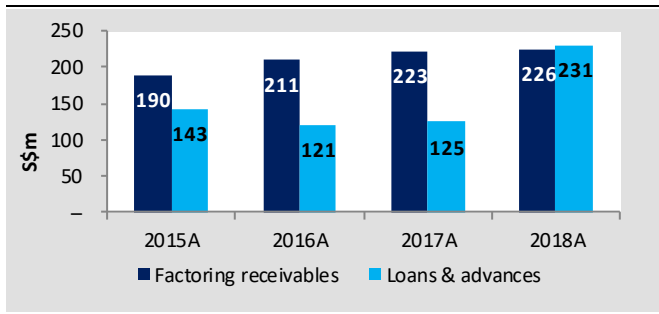
A majority of own-account workers indicated they faced difficulties, including uncertainty of finding sufficient work, according to a survey done by the Ministry of Manpower. With 9% of the respondents highlighting finance-related concerns, finance companies, especially under the new moneylending business model, is in a favorable position to better serve this growing segment of the economy.

Figure 9: Challenges faced by own-account workers in 2017, Singapore



Source: Supplementary Survey on Own-Account Workers, Manpower Research & Statistics Department, MOM

Figure 10: IFS has been growing factoring receivables 10% p.a. Loans declined YoY in 2015 and 2016 but has started to grow again.



Source: IFS Capital, KGI Research

Valuation

We maintain our Outperform recommendation on IFS in view of its rapid recovery, driven by growth in its factoring business. We assign a target price of S\$0.30 to IFS Capital, based on a FY20F P/B of 0.6x and a FY20F BVPS of S\$0.50. We believe that the worst is over for IFS and expect IFS to trade at a higher P/B, closer to its peer average as it expands its balance sheet.

Lack of comparable peers. There is a lack of direct comparable in the Singapore market in terms of funding profile. Although there are other financing companies such as Hong Leong Finance and Singapura Finance, we note that they target different segments of the market (e.g., car financing, property loans). The provision of short-term funding for SMEs makes up the majority of IFS' operating profit and growth driver.

P/B valuation more meaningful. In terms of relative valuations, P/B basis would be more meaningful as earnings-based valuations can be volatile for small-mid cap finance companies. Singapore finance companies trade at an average of 0.6x P/B against single-digit ROEs.

Key assumptions for our revenue/earnings model

- Factoring and lending business to benefit from broad-based economic growth in Southeast Asia and from a better regulatory environment.
- Growth for factoring and lending business in Singapore to remain strong. Singapore's total factoring volume grew by a CAGR of 32% from 2010 to 2016 and we expect IFS to continue benefitting from this trend.
- Thailand is the largest significant growth driver and the most profitable entity in the IFS group. In 2018, operating income and assets in the country increased by 13% YoY and 7% respectively. IFS owns a 73.1% effective stake in IFS Capital (Thailand), which is listed on the Stock Exchange of Thailand.
- Malaysia and Indonesia are expected to grow in 2019 but their contributions to the group are expected to remain minimal in the short-term. However, we are positive on their long-term prospects.
- We expect net claims from insurance business to subside after termination of certain policies (mainly auto-related) in 2017 and 2018. Going forward, credit financing segment will drive revenues while insurance segment to remain flat as the new management for ECICS Limited continues to turn it around.

Figure 11: Peer comparison of credit financing firms

Company	Last Price	Market Cap (\$m)	Return on Equity (%)			P / B (x)		Div Yield (%)		Gearing (x) Current
			FY-1	Last FY	Last FY	FY+1	FY+2	Last FY	FY+1	
IFS Capital Ltd	SGD 0.21	79	1.3	11.2	0.5	0.5	0.5	2.6	0.0	1.7
<u>Local Credit Financing Firms</u>										
Hong Leong Finance Ltd	SGD 2.69	1,203	5.0	6.5	0.6	-	-	5.9	-	1.2
Sing Investments & Finance	SGD 1.42	224	6.9	6.9	0.6	-	-	4.8	-	1.1
Singapura Finance Ltd	SGD 0.89	141	1.9	3.0	0.6	-	-	4.4	-	1.3
Average			4.6	5.5	0.6	-	-	5.1	-	1.2

Source: Bloomberg, Company Data, KGI Research

Financials

YE December

INCOME STATEMENT (SGD mn)	2017A	2018A	2019F	2020F	2021F
Interest Income	24.6	28.1	32.6	35.9	38.4
Interest Expense	(5.6)	(7.6)	(8.4)	(9.0)	(10.0)
Net Interest Income	19.0	20.5	24.2	26.9	28.4
Non Interest Income	24.0	33.4	18.4	16.5	17.8
Total Other Income	0.5	16.8	0.0	0.0	0.0
Gross Operating Income	48.2	44.8	51.1	52.4	56.2
Operating Expenses	(23.0)	(23.0)	(21.5)	(21.7)	(23.2)
Depreciation and amortisation	1.58	1.44	1.88	1.96	2.15
Profit/(Loss) after Tax	3.6	19.9	10.4	10.6	11.6
Profit/(Loss) attributable to Owners of the Company	2.0	18.0	8.3	8.5	9.3
BALANCE SHEET (SGD mn)	2017A	2018A	2019F	2020F	2021F
Number of Shares	376.0	376.0	376.0	376.0	376.0
Issued Share Capital	137.3	137.3	137.3	137.3	137.3
Shareholders Funds	152.3	169.2	177.5	186.0	195.2
Total Assets	411.0	506.5	530.1	549.6	568.4
Total Liabilities	244.7	321.9	325.5	332.8	348.2
Cash & Equivalents	35.1	48.7	65.6	77.2	81.4
CASH FLOW STATEMENT (SGD mn)	2017A	2018A	2019F	2020F	2021F
Cash from operations	(17.1)	(97.5)	5.8	0.3	(6.9)
Cash from investing	11.4	41.3	11.8	12.0	11.9
Cash from financing	6.9	69.6	(0.7)	(0.7)	(0.8)
Net increase in cash	1.2	13.4	16.9	11.6	4.2
Beginning cash	33.7	35.1	48.7	65.6	77.2
Ending Cash	35.1	48.7	65.6	77.2	81.4
KEY RATIOS	2017A	2018A	2019F	2020F	2021F
NAV per share (SGD Cents)	40.5	45.0	47.2	49.5	51.9
Price/NAV (x)	0.52	0.47	0.44	0.42	0.40
Profitability (%)					
Return on Average Equity	1.55%	11.86%	5.15%	4.91%	5.12%
Return on Average Asset	0.81%	7.80%	3.07%	2.76%	2.97%
Financial Structure					
Leverage Ratio (x)	1.6	1.9	1.8	1.8	1.8
Liquidity Ratio (x)	1.2	1.2	1.3	1.3	1.3
Total Liabilities/Total Assets (%)	59.54%	63.56%	61.40%	60.55%	61.25%

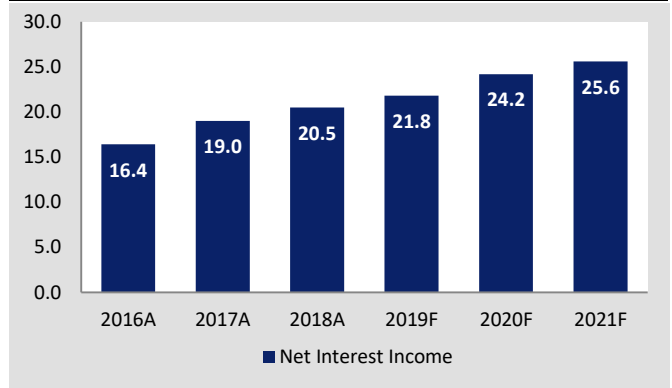
Source: Company data, KGI Research

Figure 12: Company profile

IFS Capital Limited (IFS), as a regional Group provides commercial finance services like factoring, hire-purchase/leasing, loans, government-assisted schemes and trade/export finance, to small and medium sized enterprises (SMEs). The group also provides bonds and guarantees, credit insurance and general insurance through its wholly-owned subsidiary, ECICS Limited. IFS was incorporated in Singapore in 1987 and has been listed on the Mainboard of the Singapore Exchange since July 1993.

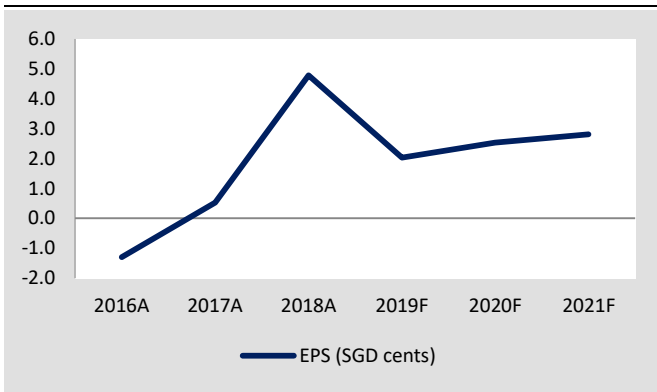
Source: Company data, KGI Research

Figure 13: Net interest income (S\$'000)



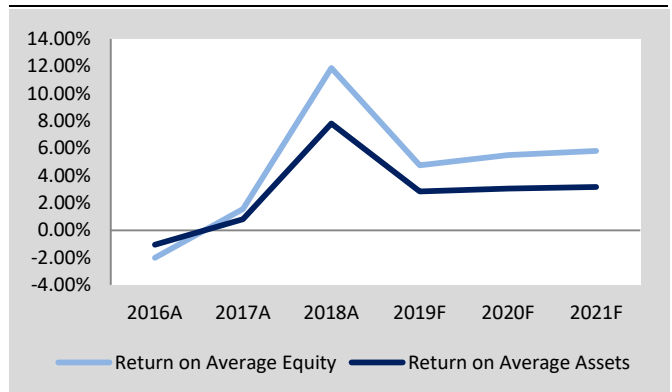
Source: Company data, KGI Research

Figure 14: EPS projections



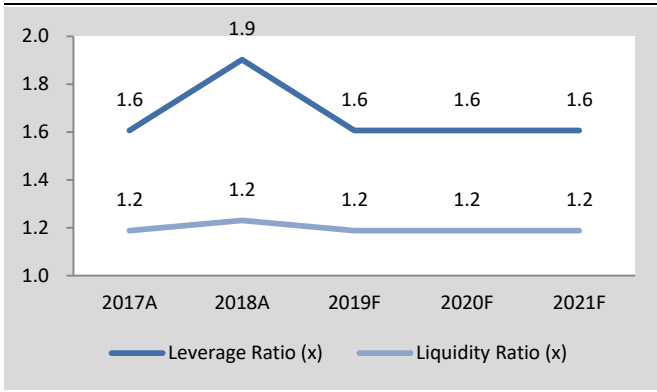
Source: Company data, KGI Research

Figure 15: ROE vs ROA



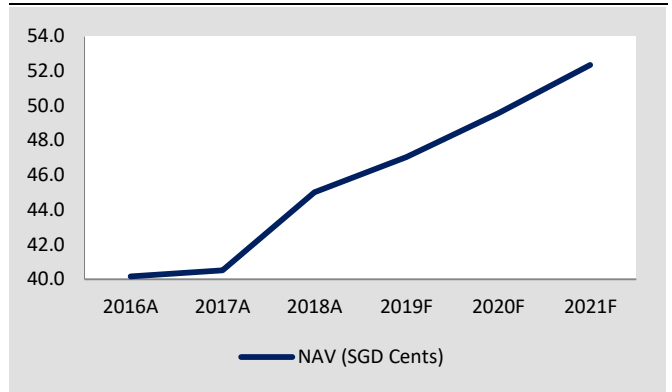
Source: Company data, KGI Research

Figure 16: Financial ratios



Source: Company data, KGI Research

Figure 17: Book value projections



Source: Company data, KGI Research

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