Stock Update

IIFL Finance Ltd.

Nov 17, 2021

RETAILRESEARCH

IIFL Finance Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
NBFCs	Rs.335.8	Buy at LTP of Rs.335.8 & add more on dips of Rs.304	Rs.371	Rs.390	2 quarters

HDFC Scrip Code	IIFFINEQNR
BSE Code	532636
NSE Code	IIFL
Bloomberg	IIFL:IN
CMP Nov 16, 2021	335.8
Equity Capital (Rs Cr)	75.8
Face Value (Rs)	2
Equity Share O/S (Cr)	37.9
Market Cap (Rs Cr)	12,733
ABook Value (Rs)	134
Avg. 52 Wk Volumes	1033529
52 Week High	375.05
52 Week Low	94.80

Share holding Pattern % (Sept, 2021)	
Promoters	24.93
Institutions	25.45
Non Institutions	49.62
Total	100.00

* Refer at the end for explanation on Risk Ratings

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Our Take:

IIFL Finance Ltd (erstwhile IIFL Holdings Ltd) is one of the leading retail focused diversified NBFCs in India, engaged in the business of loans and mortgages along with its subsidiaries IIFL Home Finance Ltd and Samasta Microfinance Ltd. The company is expecting high growth in next 2-3 years, for which it has been aggressively building the branch network and increasing employee strength. It is also spending heavy on the branding and technology. The company has strong hold on technological innovations. Recently, it has become the first NBFC in the country to launch instant unsecured business loans with an end to end journey on WhatsApp. It is also constantly strengthening the tie-ups with banks for co-lending. As of Q2FY22, 94% of the loans are retail in nature and 69% of these retail loans (excluding gold loans which are not classified as PSL loans) are priority sector lending (PSL) norms compliant, which could help IIFL Finance raise long term funds. The company is well capitalized and has diversified resources profile. In past few quarters, the company has transferred significant amount of wholesale real estate credit assets to Alternative Investment Fund (AIF). The capital released by the above transaction, will strengthen IIFL Finance balance sheet and will help it focus to sharply on retail lending, in line with its strategy.

The company is into the ASM stage-1 on the exchanges with the daily price circuit limit of 5%. It has limited seasoning of the portfolio and NPA trend during high growth phase will be important factor to track.

We had issued Initiating Coverage report on IIFL Finance on 28th April, 2021 and recommended Buy at LTP of Rs.266 and add further on dips to Rs.241 band, for base case target of Rs.290 and bull case target of Rs.319 over the next two quarters. The stock entered our add further band on 5th May, 2021. The bull case target of Rs.319 was achieved on 14th September 2021, yielding return of 25.4%.

Link for the Initiating Coverage:
https://www.hdfcsec.com/hsl.research.pdf/IIFL%20Finance-Initiating%20Coverage%20-%2028042021.pdf

Valuation & Recommendation:

IIFL Finance has posted decent Q2FY22 results with strong AUM growth across the segments. Asset quality was also stable, supported by higher collection efficiencies. The management has guided that in next three years they are expecting to double the loan book. We expect Home and Gold loans to be the key growth drivers for the company which are expected to grow at CAGR 15% and 27% respectively over FY21-24E. We have envisaged 14% CAGR in Net Interest Income and 22% CAGR in net profit over FY21-FY24E. Further, we have estimated that the loan book would grow at 13.6% CAGR over this period. We expect that asset quality and NIM could improve gradually over FY21-24E.

We feel that investors can buy IIFL Finance at the LTP of Rs.335.6 (1.76x Sep-23E ABV) and add on dips to Rs.304 (1.6x Sep-23E ABV) band. We expect the Base case fair value of Rs.371 (1.95x Sep-23E ABV) and the Bull case fair value of Rs.390 (2.05x Sep-23E ABV) over the next 2 quarters.

Financial Summary

Particulars (Rs Cr)	Q2 FY22	Q2 FY21	YoY (%)	Q1FY21	QoQ (%)	FY20	FY21	FY22E	FY23E	FY24E
NII	598.2	562.9	*6.3*	544.1	*9.9*	1639	2084	2363	2726	3114
PPOP	582	581	*0.2*	516	*12.8*	749	1526	2048	2392	2730
PAT	291.6	212.6	*37.2*	265.8	*9.7*	554	761	907	1171	1379
EPS (Rs)						14.6	20.1	23.9	30.9	36.4
ABV (Rs)						119.8	134.4	152.1	175.7	204.8
P/E (x)						22.9	16.7	14.0	10.9	9.2
P/ABV (x)						2.8	2.5	2.2	1.9	1.6
RoAA (%)						1.6	2.0	2.1	2.5	2.6

(Source: Company, HDFC sec)

Recent Developments

Q2FY22 Result Update

During the quarter, the consolidated Net Interest Income (NII) grew by 6%/10% YoY/QoQ. Operating profit remained flat YoY at Rs.582 Cr. NIM improved to 7% compared to 6.6% in the last quarter. Due to high operating expenses Cost to Income ratio reached 40% compared to 33.6% YoY. Net profit rose by 37% to Rs.292 Cr due to lower loan loss provisions.

IIFL Finance had loan assets under management (loan AUM) of Rs 44,249 Cr as at September 30, 2021, with the home loans segment constituting 35%, gold loans 31%, business loans 16% and microfinance loans 10% of the total AUM. Out of these, only business loan segment posted muted YoY growth, all other business growth remained robust. During the quarter, disbursements were back to pre-covid levels with heightened economic activity. Liquidity is now at all-time high at Rs.6,379 Cr. IIFL Home Finance wholly owned subsidiary reported a PAT of Rs. 153Cr for Q2FY22 and in H1FY22 its PAT stood at Rs. 300Cr v/s a PAT of Rs.401Cr for entire FY21. Disbursements for Home loans for the quarter stood at Rs. 1596Cr up 84/61% on a YoY/QoQ basis.

Guidance

Management has informed that they are betting aggressively on growth for which they have increased net manpower by 15% in the quarter itself; 230 new branch counts was added during the quarter. Besides, they have accelerated investment in technology and branding. Further, co-lending proposition is getting very positive response from banks. For H2FY22, the management has guided for 10% to 12% growth in the loan book. Further, the long term plan is to double the loan book in next three years while maintaining the maintaining return ratios at the current level. Cost to income ratio should reach around 33% to 35% in the same time frame, however we feel that in the short term this could go northwards looking at the aggressive branch, employee, branding and technological expansion.

Asset Quality

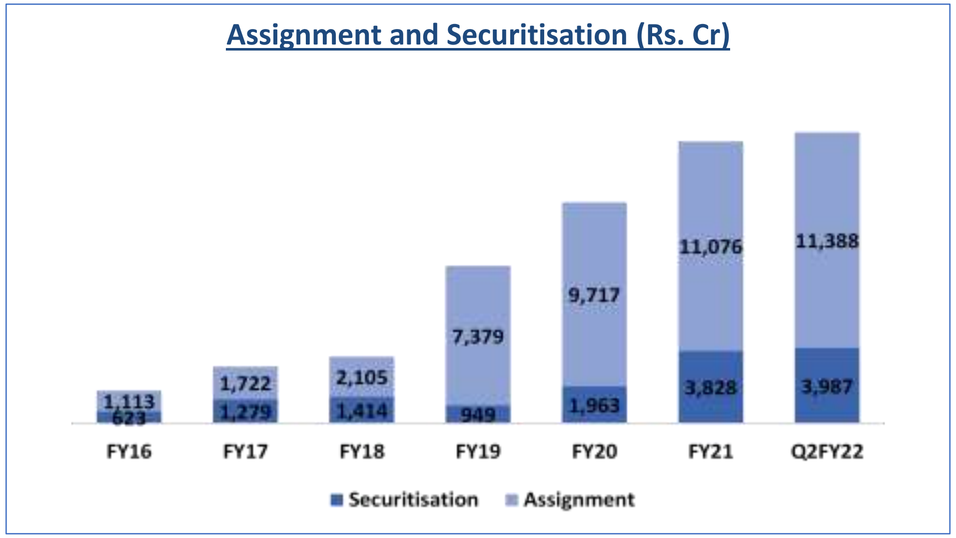
On the asset quality front, the GNPA stood at 2.3% and NNPA stood at 1.1% compared to 2.25% and 1% respectively in the last quarter. As per IND-AS accounting provision coverage of NPA stood at 175%. The collection efficiencies improved significantly. Except for business loan segment, all other segments reported almost to 100% collection efficiency. Even in the business loan segment the collection efficiency improved to 94% vs 84% in last quarter.

Segment Detail Q2FY22

Particulars	% AUM Share	AUM (Rs. Cr)	YoY%	QoQ%	GNPA %	NNPA%	Portfolio Yield%	Portfolio average Ticket Size (Rs. Lakhs)	Collection Efficiency trends (%)
Home Loans	35%	15698	22%	6%	1.8%	1.1%	10.1%	17	99%
Gold Loans	31%	13600	19%	3%	1.0%	0.8%	17.3%	0.7	101%
Business Loans	16%	7019	-11%	-1%	6.1%	2.5%	15.4%	10.8	94%
Microfinance	10%	4534	31%	3%	2.4%	0.0%	22.3%	0.2	106%
Construction & Real Estate	6%	2722	-39%	-3%	1.6%	1.1%	16.2%	3641.4	
Capital Market Finance	2%	676	-7%	-20%	0.0%	0.0%	11.9%	142.8	
Total	100%	44249	8%	3%	2.3%	1.1%	14.8%		

Assignment and Securitisation

It is noteworthy that IIFL Finance's large proportion of loans iscompliant with RBI's priority sector lending (PSL) norms. As of Q2FY22, 94% of the loans are retail in nature and 69% of these retail loans (excluding gold loans which are not classified as PSL loans) are PSL compliant. The large share of retail and PSL-compliant loans are of significant value as the Company can sell down these loans to raise long-term resources. As of H1FY22, the company has assigned asset size of Rs.11,388 Cr and securitized book stood at Rs.3,987 Cr on the total AUM of Rs.44,249 Cr. In case of assigned assets all credit risk lies with the bank while IIFL enjoys the spread on it.



Tie-ups with banks

The company has formed strategic alliances and partnerships with reputed banks and also some FinTech companies for co-lending and loan assignments. These partnerships can help the company leverage its geographical reach, servicing capabilities, underwriting skills and trained workforce, and combine that with the bank's capital balance sheet and risk taking capability and have a win-win relationship. Banks are always keen to buy retail loan portfolio or build the same by co-lending. IIFL Finance, with its unique strengths in scaling up co-lending with banks, can achieve superior return on capital and grow faster without liquidity stress. As of now, the company has done partnership with Central Bank of India, ICICI Bank, Standard Chartered, DCB Bank, Shivalik Small Finance Bank and Punjab National Bank. During the last quarter, the company has also launched co-branded prepaid card with ICICI Bank for gold loan customers. It has also tie-up with GooglePay for lead generation.

Digital focus

The company has been constantly investing in digital platforms since past couple of years. Now the company has completely paperless and cashless services, right from customer on-boarding, underwriting and loan disbursement to collection. It has partnered with fintech players, under the 'IIFL Disrupt', to accept online payments via UPI platforms. It also has a customer-facing mobile application facilitating service and support related tasks for the users' existing loan accounts and to apply for new loans as well. IIFL Finance has till date disbursed Rs.43 Cr via My Money app.

IIFL Finance has become the first NBFC in the country to launch instant unsecured business loan end to end journey on WhatsApp. Up to Rs.10 lakh worth of loan is eligible on WhatsApp. It is also allowing users to verify their bank details using RBI-backed "Account Aggregator". 60000+ leads were generated in 10 days of launch and loan worth Rs.4.5 Cr was disbursed.

Well capitalised

IIFL Finance is well capitalised and looking at the growth strategy, it will not require to raise capital in the foreseeable future. As of Q2FY22, the capital adequacy ratio stood at 25.9% and tier-1 at 18.3%; these are well above the statutory requirement of 10% and 15% respectively. Total capital ratio of home finance was at 30.7% and for microfinance stood at 21.9%.

During the quarter the company has raised Rs.3,717 Cr through term loans and refinance and in addition loans worth of Rs.3,655 Cr was securitized/ assigned during the quarter. The total liquidity as of September 30, 2021 stands at Rs.6,379 Cr. Additionally, it has raised Rs.843 Cr by way of public issue of long-term secured bonds in the month of October 2021. IIFL Home Finance also had public issue of a subordinate debt and raised Rs.656 Cr in the month of July. Further, the company has positive ALM across all the time buckets. In the past, the company has raised significant amount of money from marquee investors like Fairfax group, CDC Group PLC and other foreign investors, which demonstrates its ability to raise funds as and when required.

Transfer of real estate credit assets to AIF

Construction and Real Estate finance segment of the company includes loans to developers for construction and development of predominantly affordable residential projects and a small proportion of mixed-use projects. In line with the broader retail strategy, the construction finance vertical is an enabler for providing retail loans under the approved project route, the Company has tie-ups with developers for funding the property buyers under the retail home loan category. IIFL Finance is planning to transfer substantial part of this segment's loan assets in the form of non-convertible debentures to an Alternative Investment Fund (AIF) wherein, the Company will continue to own at least a third of the AIF's units. A significant part of this was already sold during the quarter ended June 30, 2021. The AIF which was formed in May '21 was of the size of Rs. 3600Cr comprising of all the wholesale portfolio of real estate loans. It had signed with Ares SSG Capital Management which had committed an investment of Rs. 1200Cr towards units in the AIF. The capital released by the above transaction, will strengthen IIFL Finance balance sheet and help it focus sharply on retail lending, in line with its strategy.
There has been a reduction in the real estate book to 6% of the assets under management as on Sept 30, 2021 (13% as on September 30, 2019) and 46% of the net worth (103% as on September 30, 2019).

Strong physical and digital footprint

Over the years the company has steadily built the strong physical as well as digital presence and over last couple of quarters it has been aggressively expanding its reach. Physical presence is required in the gold and micro finance business whereas a digital identity provides wider access in the home, personal and MSME loan categories. Currently the company has 2,914 branches and 23,775 employees of which 350 branches and nearly 4,000 employees were added during H1FY22. The branch network is well spread across Tier I/II and Tier III cities across the country, effectively providing credit to the underserved segments of customers in these areas. The microfinance branches are well entrenched in rural and semi-urban areas as well, effectively serving the relevant customer segments. Further, the management has informed that they are planning on adding 700 branches in next 12-18 months for gold loans as they are seeing good demand.

For the digital presence, the company has in place advanced technology led systems for loan applications through the website and portable tablet based applications. This caters to the growing section of population which prefers or is incrementally relying on digital channels to access services. The cross-country branch presence coupled with well-developed digital infrastructure gives a widespread presence across channels and enables the company in accessing and servicing a diverse customer base and their multiple credit requirements.

Risks & Concerns

- As stated in the initiating coverage also, the company has limited seasoning in the some of the assets as they are relatively newly launched. They have not tested the complete credit cycle.
- High competition from banks or peer NBFCs could impact the growth rate.
- The company is expecting high growth in next 2-3 years, for which it has been aggressively building the branch network and increasing employee strength. It is also spending heavy on the branding and technology. This could impact the cost to income ratio of the company in the near term. Moreover, the asset quality trend during this high growth phase will be a key monitorable.
- Slower-than-expected pick-up in the economy may impact the AUM growth for the company. Lower-than-expected loan growth and more-than-expected deterioration in asset quality remain key risks to our thesis.
- Higher region-wise concentration as ~45% of the outstanding pool principal is from Gujarat, Maharashtra and Telangana.

Company Background:

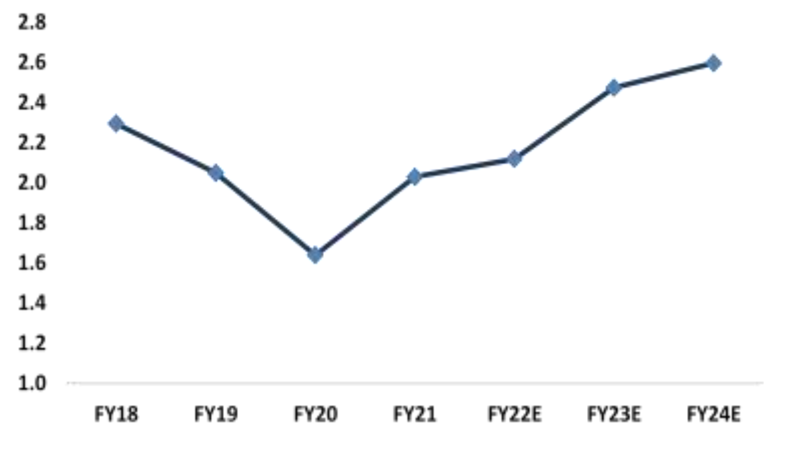
IIFL Finance Ltd is one of the leading retail focused diversified NBFC in India, engaged in the business of loans and mortgages along with its subsidiaries - IIFL Home Finance Limited and IIFL Samasta Finance Limited. IIFL Finance, through its subsidiaries, offers a wide spectrum of products such as Home loan, Gold loan, Business loan, Microfinance, Capital Market finance and Developer & Construction finance to a vast customer base of over 6 million customers. IIFL Finance has widened its pan-India reach through extensive network of branches spread across the country and various digital channels.

IIFL Finance (erstwhile IIFL Holdings Ltd) was the holding company for the entire IIFL group. As a part of corporate restructuring, the securities and wealth businesses of IIFL Holdings Ltd were demerged into IIFL Securities Ltd and IIFL Wealth Management Ltd respectively.

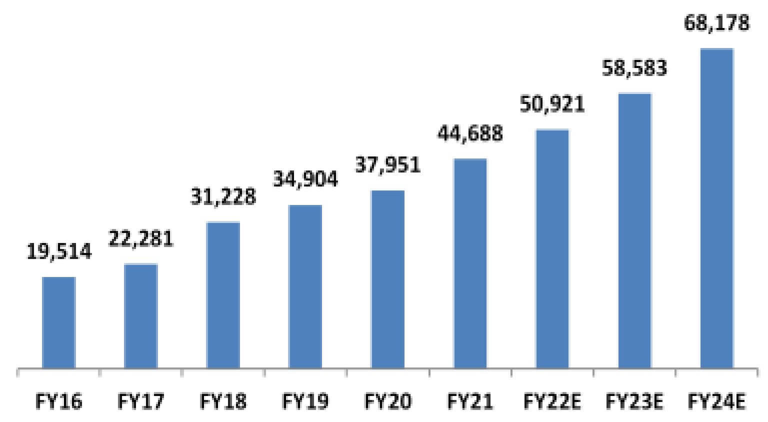
IIFL Holdings Ltd was renamed IIFL Finance Ltd and now is the holding company for the lending businesses of the IIFL group with effect from 30 March 2020.

IIFL Finance's loan book was tilted towards the business loans and real estate, which gradually was reduced and focus was changed for building retail assets mix. The commercial vehicles' financing business was sold as a as a going concern in FY21. Now, the company has wide product portfolio of Affordable Home Loans, Gold Loans, Business Loans and Microfinance which caters to all types of customers in the country – salaried, self-employed, informal sector, HNIs and corporates.

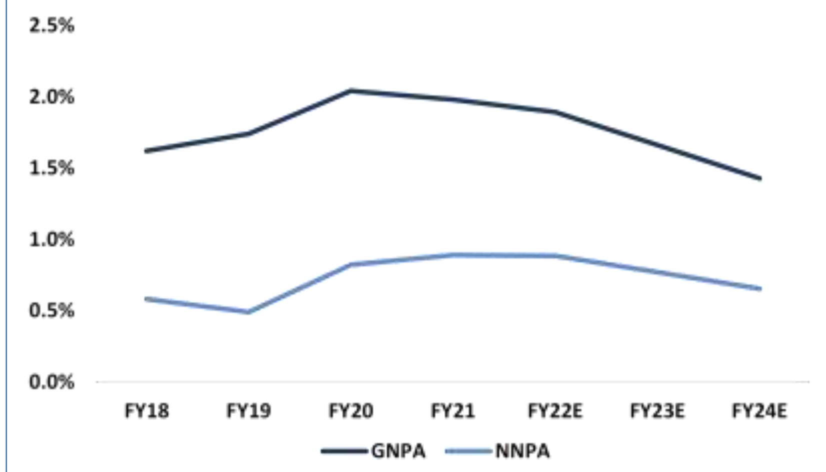
RoAA (%)



AUM to grow at 13.6% CAGR over FY21-24E



NPA Trend



Financials

Income Statement

(Rs Cr)	FY20	FY21	FY22E	FY23E	FY24E
Interest Income	4043.5	4709.7	5290.6	5912.6	6641.2
Interest Expenses	2405.0	2625.8	2927.8	3186.1	3526.9
Net Interest Income	**1638.5**	**2083.9**	**2362.8**	**2726.5**	**3114.3**
Income from assigned assets	575.8	702.0	1000.0	1100.0	1200.0
Non-interest income	307.2	578.0	661.3	688.5	691.8
Operating Income	**2521.5**	**3363.9**	**4024.1**	**4514.9**	**5006.1**
Operating Expenses	1773.0	1838.3	1976.4	2122.7	2276.1
PPP	748.6	1525.6	2047.7	2392.3	2729.9
Prov & Cont	23.0	520.3	822.2	809.9	853.2
Profit Before Tax	725.6	1005.3	1225.5	1582.3	1876.7
Tax	171.8	244.0	318.6	411.4	497.3
PAT	**553.8**	**761.3**	**906.9**	**1170.9**	**1379.4**

Balance Sheet

(Rs Cr)	FY20	FY21	FY22E	FY23E	FY24E
Share Capital	75.7	75.8	75.8	75.8	75.8
Non-controlling interest	5.6	5.9	5.9	5.9	5.9
Reserves & Surplus	4684.3	5311.7	6048.1	7010.6	8181.5
Shareholder funds	**4765.6**	**5393.4**	**6129.8**	**7092.3**	**8263.2**
Borrowings	27783.4	32367.0	35722.3	39245.7	44728.7
Other Liab & Prov.	1822.3	2906.7	3127.3	3365.9	3594.6
SOURCES OF FUNDS	**34371.4**	**40667.1**	**44979.4**	**49703.8**	**56586.5**
Fixed and Other Intangible Asset	609.3	695.2	657.8	687.8	687.8
Investment	770.4	31.5	303.7	344.3	393.7
Cash & Bank Balance	3215.9	4784.0	4537.3	4004.0	4428.7
Advances	28534.6	33533.1	37962.1	43032.5	49206.5
Other Assets	1240.3	1622.9	1518.5	1635.2	1869.8
TOTAL ASSETS	**34370.5**	**40666.7**	**44979.3**	**49703.8**	**56586.5**

(Source: Company, HDFC sec)

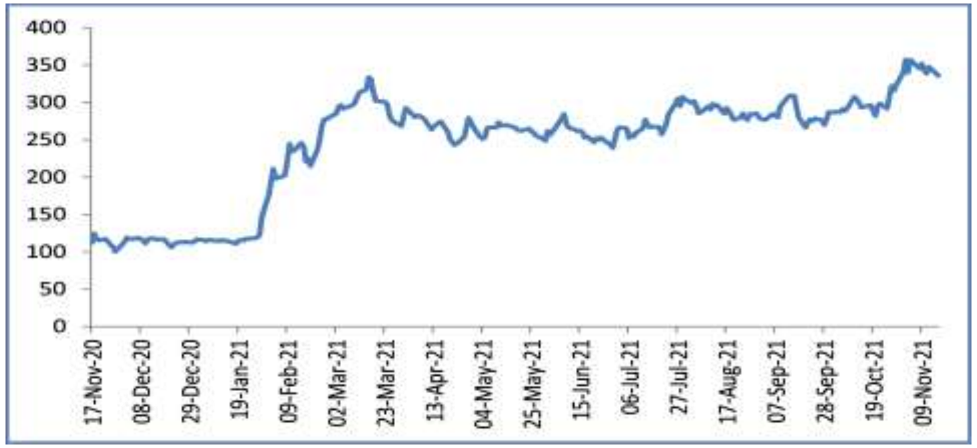
Key Ratio

	FY20	FY21	FY22E	FY23E	FY24E
Return Ratios					
Calc. Yield on adv	14.5%	15.2%	14.8%	14.6%	14.4%
Calc. Cost of borr	8.7%	8.1%	8.2%	8.1%	7.9%
NIM	5.9%	6.7%	6.6%	6.7%	6.8%
RoAE	12.1%	15.0%	15.7%	17.7%	18.0%
RoAA	1.6%	2.0%	2.1%	2.5%	2.6%
Asset Quality Ratios					
GNPA	2.0%	2.0%	2.0%	2.0%	2.0%
NNPA	0.8%	0.9%	1.0%	1.0%	1.0%
PCR	60%	55%	52%	50%	49%
Growth Ratios					
Advances	4.2%	17.5%	13.2%	13.4%	14.3%
Borrowings	4.3%	16.5%	10.4%	9.9%	14.0%
NII	-14.9%	27.2%	13.4%	15.4%	14.2%
PPP	-46.3%	103.8%	34.2%	16.8%	14.1%
PAT	-30.5%	37.5%	19.1%	29.1%	17.8%

Key Ratio

	FY20	FY21	FY22E	FY23E	FY24E
Valuation Ratios					
EPS	14.6	20.1	23.9	30.9	36.4
P/E	22.9	16.7	14.0	10.9	9.2
Adj. BVPS	119.8	134.4	152.1	175.7	204.8
P/ABV	2.8	2.5	2.2	1.9	1.6
Dividend per share	2.3	3.0	4.5	5.5	5.5
Dividend Yield (%)	0.7	0.9	1.3	1.6	1.6
Other Ratios					
Cost-Income	70.3	54.6	49.1	47.0	45.5
Leverage	7.2	7.5	7.3	7.0	6.8

One Year Price Chart



HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicality of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

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