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20 YEARS

Initiating Coverage

IIFL Wealth Management Ltd.

19-July-2021

RETAIL RESEARCH

IIFL Wealth Management Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
BFSI - NBFC	Rs 1388.9	Buy at LTP and add on dips to Rs 1220-1225 band	Rs 1523	Rs 1642	2 quarters

HDFC Scrip Code	IIFLWEALTH
BSE Code	542772
NSE Code	IIFLWAM
Bloomberg	IIFLWAM IN
CMP Jul 16, 2021 (Rs)	1,388.9
Equity Capital (cr)	17.6
Face Value (Rs)	2
Eq. Share O/S (cr)	8.8
Market Cap (Rs cr)	12,214.7
Adj. Book Value (Rs)	321.8
Avg.52 Wk Volume	54,083
52 Week High (Rs)	1,440.0
52 Week Low (Rs)	856.9

Share holding Pattern % (Jun, 2021)	
Promoters	22.92
Institutions	65.00
Non Institutions	12.08
Total	100.0

Fundamental Research Analyst
Atul Karwa
atul.karwa@hdfcsec.com

Our Take:

IIFL Wealth Management Ltd. (IWML) is among the largest Non-Bank wealth management firms in India with a closing AUM of over Rs 2 lakh crore as of FY21. The company has grown over the years organically as well as inorganically with an AUM CAGR of ~25% over FY15-FY21. IWML's few sizeable acquisitions includes 1) L&T Finance capital market business in 2019 and 2) Wealth Advisors India based in Chennai. With only 9% of the wealth professionally managed and the number of HNIs expected to almost double from FY20 to FY25, provides a huge scope for wealth management firms to grow. IWML is transitioning from distribution commission based model to the more stable recurring revenue model which provides better visibility for the future. Within annual recurring revenue (ARR), it aims to scale-up the IIFL One and the AIF driven AMC business. Cost control initiatives undertaken in the last 12-18 months should result in higher profitability. Low capital requirement and high dividend payouts render it attractive to shareholders. The company has been targeting an absolute RoE of 19-20% by FY23 from current 14.1% RoE (excluding goodwill) along with continuation of aggressive dividend pay-out policy of 60-80%. The company has also guided an average AUM growth of CAGR 20% over FY21-23E.

Valuation & Recommendation:

We expect total income of the company to increase at 14.7% CAGR over FY21-FY23 driven by strong growth in recurring revenue assets. PAT is expected to grow at 19.2% CAGR resulting from the cost saving initiatives taken by the company in the last 12-18 months. RoE (excl. goodwill) is likely to expand from 14.1% in FY21 to 19.9% in FY23. Due to buoyant capital markets, investors could park a part of their profits/wealth with wealth management companies like IWML; this could lead to a faster growth in AUM. Investors can buy the stock at LTP and add on dips to Rs 1,220-1,225 (20.5x FY23E EPS) for a base case fair value of Rs 1,523 (25.5x FY23E EPS) and bull case fair value of Rs 1,642 (27.5x FY23E EPS) in the next two quarters.

Financial Summary

Particulars (Rs cr)	Q4FY21	Q4FY20	YoY-%	Q3FY21	QoQ-%	FY20	FY21P	FY22E	FY23E
Total Income	288	178	*61.8*	280	*2.9*	851	1053	1231	1386
APAT	104	-2	*-5005.6*	97	*8.2*	202	370	449	525
Diluted EPS (Rs)	11.9	-0.2	*-4963.8*	11.0	*7.9*	23.2	42.0	51.1	59.7
P/E (x)						59.8	33.0	27.2	23.3
P/BV (x)						4.0	4.3	4.1	4.0
RoAA (%)						1.8	3.4	5.1	5.8

(Source: Company, HDFC sec)

Recent triggers

Q4FY21 financials

Core revenues of the company increased marginally to Rs 266cr in Q4FY21 driven by 13.4% growth in recurring revenues while transactional revenues contracted 8.7%. Recurring revenue assets (ARR) surged by 62.9% to Rs 1.02 lakh crore while transactional/brokerage assets (TBR) increased 11.4% to 1.05 lakh crore. However margins contracted by 18/8 bps respectively to 67/39 bps. Net flows rebounded to Rs 5,809cr aided by one ~Rs 1,500-2,000cr of institutional mandate. It is targeting net flows of Rs 20,000-25,000cr in FY22. IIFL-One assets continued to gain traction, with AUM up 8% sequentially to Rs 27,940cr.

PAT grew by 8.2% sequentially to Rs 104cr on back of lower employee costs. IWML had reported a loss of Rs 2cr in Q4FY20 which was impacted by Covid related lockdown. The company is looking to increase ARR share to 70-75% over the next 12-18 months from ~50% currently. IIFL-ONE share will rise to 50-55% of ARR by the end of FY22.

Long-term triggers

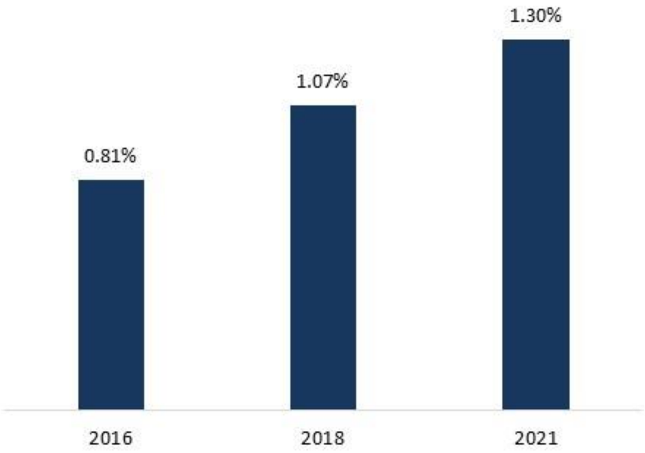
Highly under-penetrated industry – huge opportunity

The wealth management industry in India grew at a whopping 23% CAGR from 2016-2018 to $2.2tn and at 10% CAGR from FY18 to FY21. This rate of growth is more than 3x the global growth rate due to lower base and faster growth in number of HNIs in India.

Global Wealth growth

India Wealth Growth

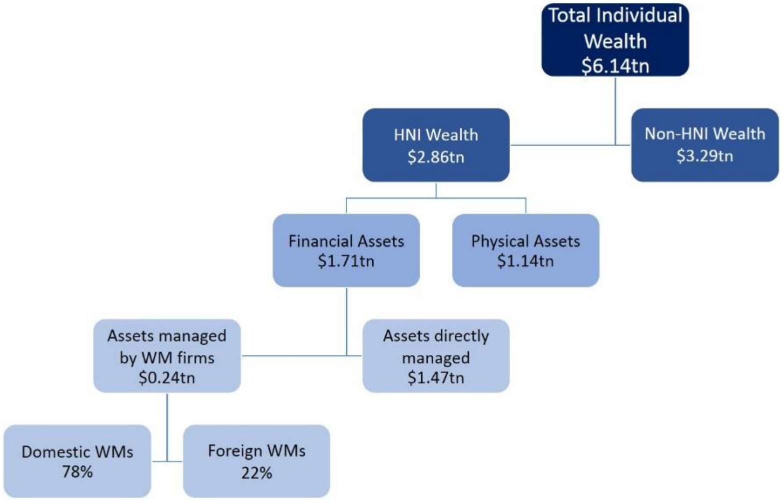
India's share in Global Wealth

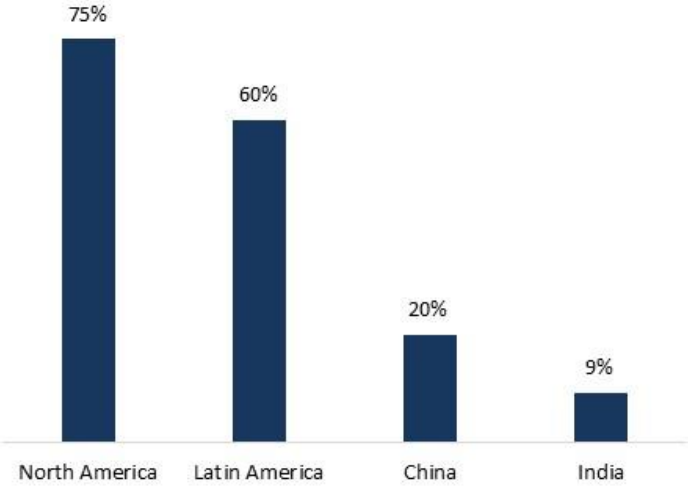


(Source: Knight Frank, HDFCsec)

Traditionally wealth was privately managed and invested in traditional products like real estate and gold. However, with the increase in investment avenues providing better returns, complexity in investment has also increased. This has brought the role of wealth managers to the fore to help clients sail through their financial journey. Currently, professionally managed assets account for only ~9% of the financial assets in India, while that number stands at ~75% in North America. As India continues its journey towards becoming a developed economy, the wealth management industry is expected to gain a larger share of financial assets and bring those under its management.

Only 9% of wealth professionally managed in India

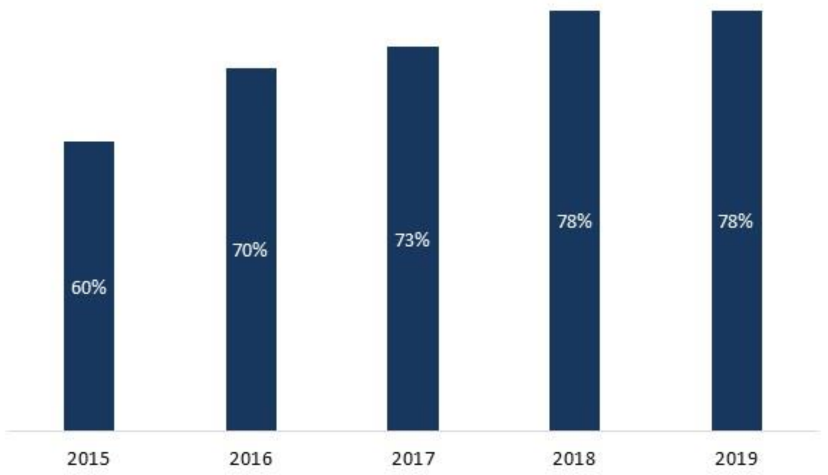




(Source: Company, HDFCsec)

The share of domestic wealth managers in the Indian wealth management has been increasing over the last few years indicating the confidence of HNIs on domestic firms.

Domestic wealth management firms improving market share

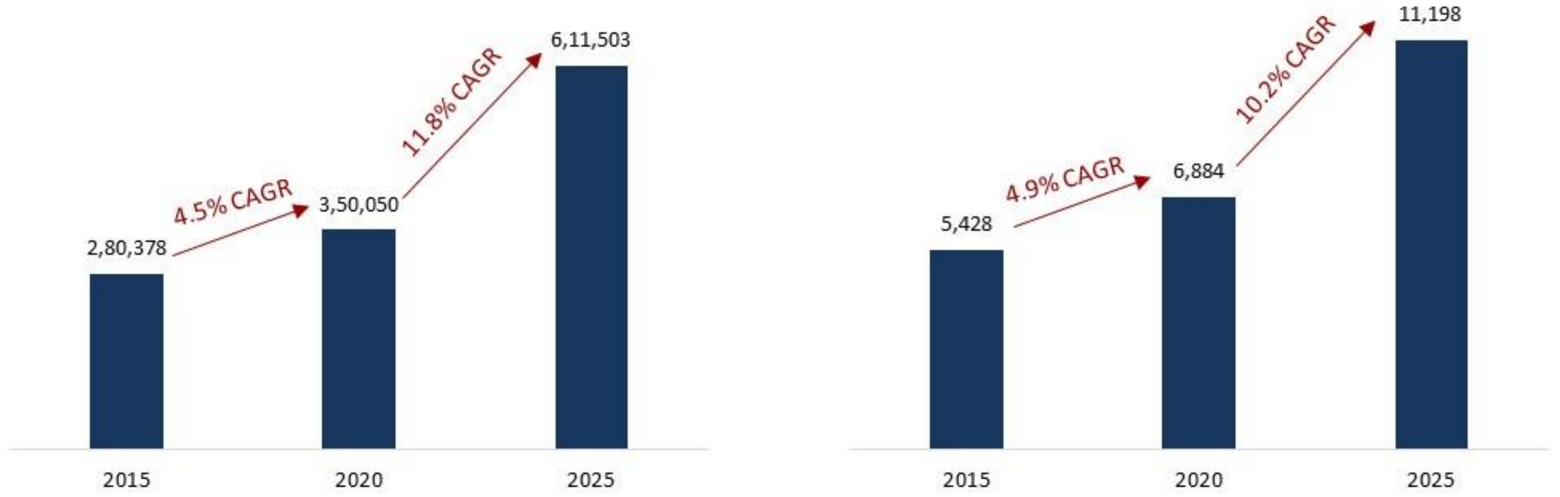


(Source: Asian Private Banker)

Expanding number of HNIs to widen opportunity pool

The Wealth Management industry in India has evolved significantly in the last decade. With a booming economy, India's wealth creation journey has accelerated over the past few years. The demographic trends in India suggest that there is high growth in the number of individuals who move upwards from middle income to upper middle income or to upper-income groups. According to 'The Wealth Report 2021' by Knight Frank the pace of growth in high networth individuals (HNIs) and ultra-high networth individuals (UHNIs) is expected to double over FY20-FY25. The number of HNIs/UHNIs grew at a CAGR of 4.5/4.9% over FY15-FY20 to 3.5/0.07 lakh. The number is expected to grow at CAGR of 11.8/10.2% over FY20-FY25 to 6.1/0.11 lakh.

Growth in HNI and UHNI to double

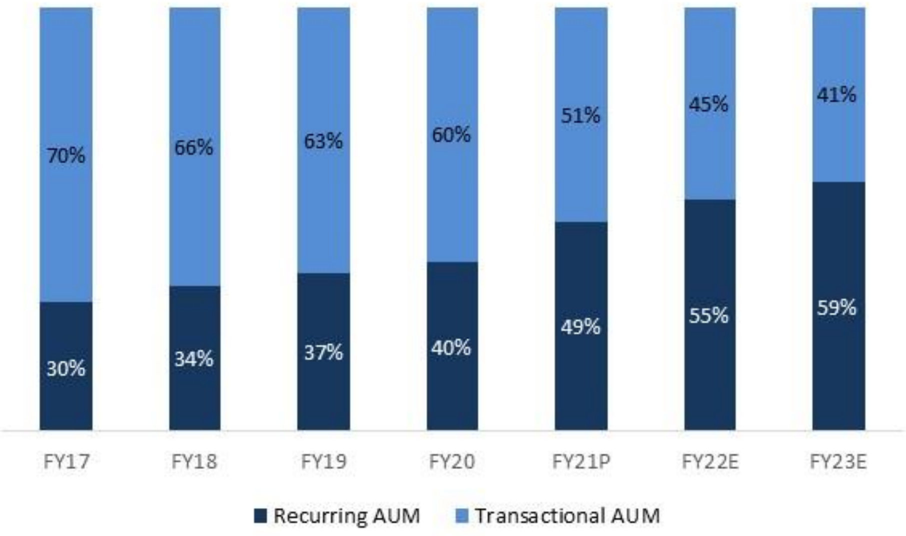


(Source: Knight Frank, HDFCsec)

Increasing share of recurring revenue assets

IWML is focusing on increasing its recurring revenue as it is more predictable and stable. The non-recurring revenue is dependent on transaction volumes. IWML had acquired L&T Finance Holdings' wealth management business for Rs 2.3bn in 2019. This gave the company access to an AUM of Rs 100bn with over half of it coming through recurring revenue assets (ARR) which was a strategic need for the company**.** The company had moved to the trail commission model even before the ban on upfront commission announced by SEBI. In 2019 the company launched a new platform IIFL One which institutionalises a range of investment options for clients under a competitive and transparent fee structure. It is an aggregation of product expertise, active advice and discretionary services provided by the company. Under IIFL-One, the company earns annual wealth management fees from clients instead of distributor commissions. This has made the fees charged more transparent. The entire transition to the new platform is expected to conclude in the next 3-5 years.

AUM breakup



(Source: Company, HDFCsec)

In contrast to earlier times, clients today are ready to pay fees for wealth management services as indicated by the strong growth in IIFL-One Assets. In FY21 IIFL-One assets grew by 58% to Rs 27,940cr. The company expects IIFL One Assets to grow at 50-55% p.a. over the next couple of years as it gradually shifts clients from distribution model to trail commission model. Also a large part of the new AUM signed by the company comes under this program.

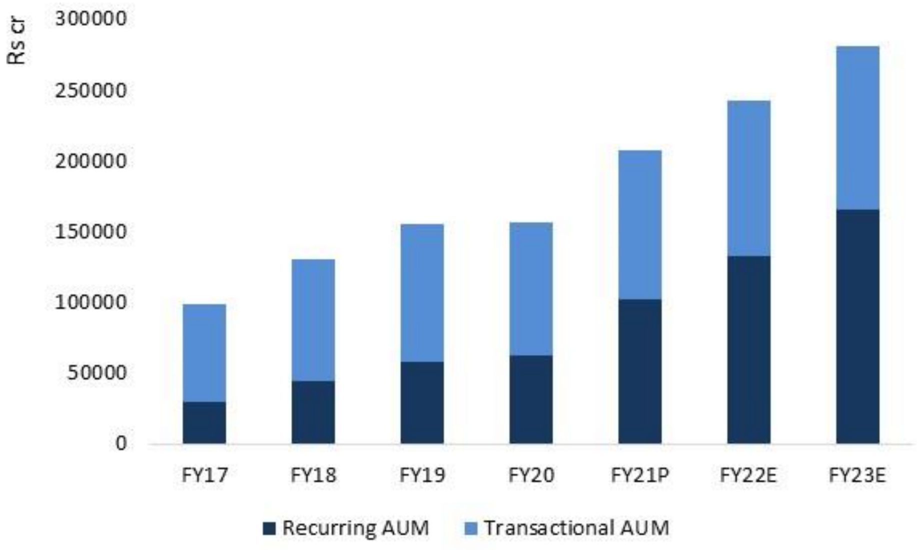
IIFL-One program gaining strength

(Source: Company, HDFCsec)

Robust business model

IWML is one of the largest and fastest growing wealth management firms in India with a presence in both – fee paying and transaction income. The annual recurring revenue model is non-cyclical and provides a stable revenues. Its AUM has grown at CAGR of 43% over FY15-FY21 to Rs 101,969cr. On the other hand the transaction business has grown at CAGR of 16% to Rs 105,074cr. Revenues in the transaction business are dependent on transaction volumes which in turn is dependent on the market conditions. However, it having a presence in both the forms de-risks the business.

20% CAGR AUM growth over FY17-FY21



(Source: Company, HDFCsec)

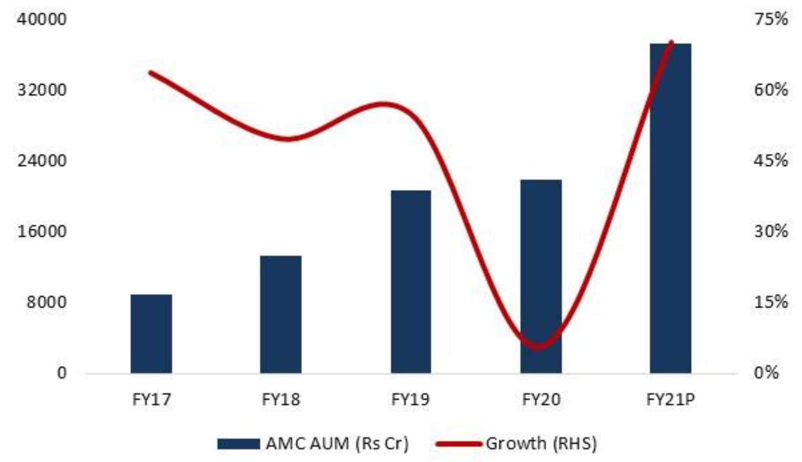
Strong market position in wealth management

IIFL Wealth offers advisory, asset management, broking and distribution services to high net worth individuals (HNIs) and ultra HNIs. Its leading market position is reflected in the assets under advice, management and distribution of ~Rs Two lakh crore as of FY21. It is also one of the largest managers of AIFs with assets under management (AUM) of Rs 23,700cr. It has a subsidiary, IIFL Wealth Prime Limited (IWPL), which is a non-banking financial company (NBFC) that provides loans against securities to the clients of the wealth management business with a loan book of ~Rs 2,500cr. The company has a presence in wealth management across nine geographies with 31 offices and 297 relationship managers as on H1FY21.

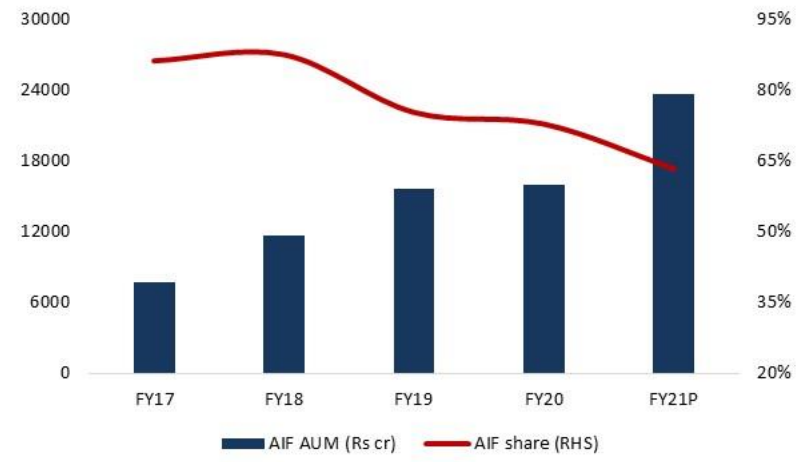
AMC business (including AIF) gaining traction

IIFL AMC has been playing a pivotal role in the growth of the Alternate Investment Fund (AIF) industry in India. Unlike other AMCs in India that are mutual fund heavy, IIFL AMC's business has maximum contribution from AIFs. As of FY21, IIFL AMC's AUM stood at Rs 37,372cr, a 70% increase over the previous year. AIFs contributed 63% to the AUM. Over the last five years from FY16 to FY21, the AUM of the AMC business has grown at a CAGR of 47% and the AIF AUM has grown at 42%.

Traction in AMC business…



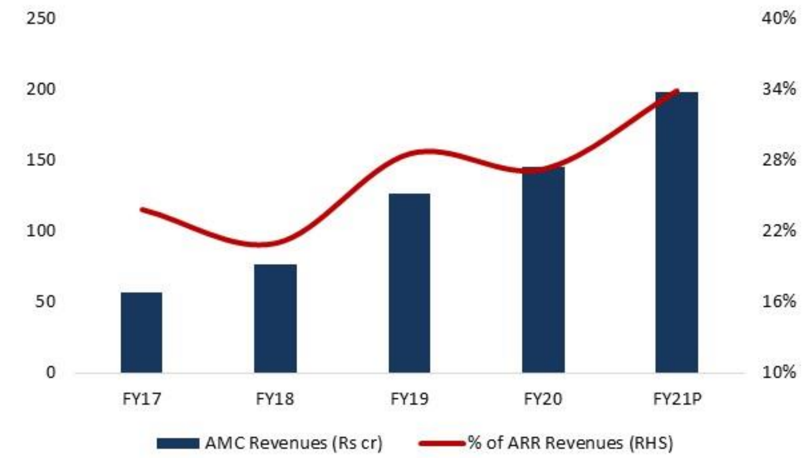
…driven largely by AIF growth



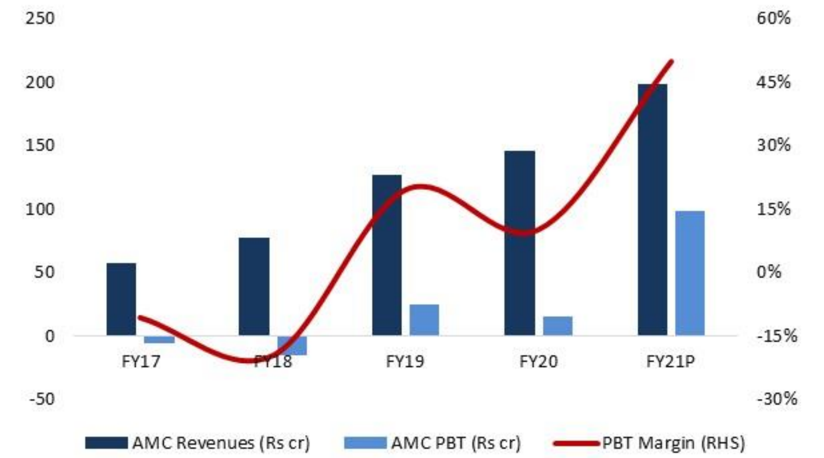
(Source: Company, HDFCsec)

Revenues from the AMC business have grown at 28% CAGR over FY 16 to FY21 and now account for 34% of the annual recurring revenues. Profitability of the business has also increased significantly with PBT margin of 50% in FY21 against 10% in FY20 and 20% in FY19.

Increasing share of AMC business



with strong profitability growth



(Source: Company, HDFCsec)

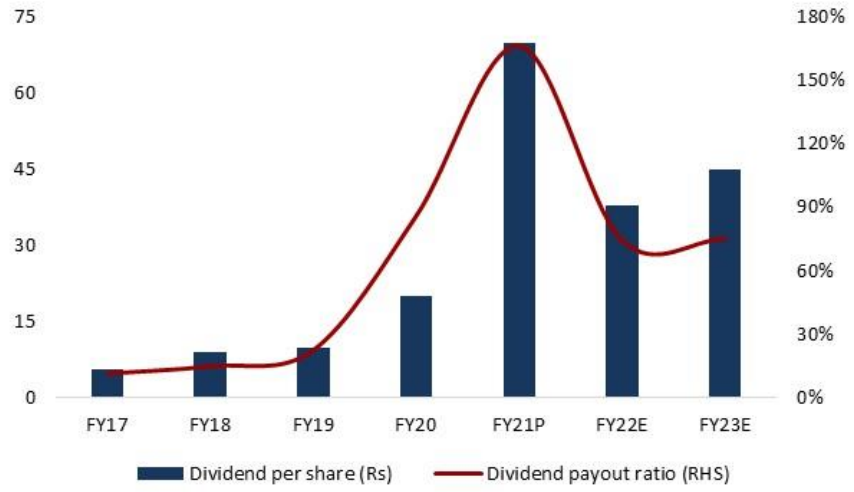
Cost controls to drive higher profitability

We expect revenues of the company to increase by at CAGR of 14.7% over FY21-FY23 driven by 27.5% growth in ARR while transactional assets growth to remain subdued at 5%. The company has taken various cost optimization initiatives over the last 12-18 months. Consequently, cost to income ratios is expected to improve from ~54% in FY21 to below 50% by FY23 thereby driving higher margins and RoEs. The management intends to achieve 20% RoE over the next few years.

High dividend payout

The company is mainly present in fee-based businesses wherein the capital requirement is relatively lower. As a result the IWML pays out a significant portion of its profits in the form of dividends. The company's stated dividend policy is to pay 50-75% of its annual profits as dividends. Since the company distributes most of its profits it is beneficial to investors who wish for regular dividends. We expect the company to pay ~75% of its profits as dividends.

Consistent dividend payout



(Source: Company, HDFCsec)

What could go wrong?

Regulatory risk in wealth management business

The wealth management business is exposed to regulatory risks in terms of types and capping of fees it can charge to its clients. Any sudden regulatory change could impact its profitability like it did in FY20 when SEBI banned upfront commission in distribution of MF products.

Volatility in equity markets

A part of the returns generated by the company for its clients is dependent on stock price movements. Continued volatility in equity markets would lead to a slowdown in inflows as investors would take a ‘wait and watch’ approach.

IIFL-One not taking off as planned

IWML is looking to transition its asset management business to fee-based model under its IIFL-One brand over the next 3-5 years. However, if this transition were to not go as planned, it could impact derisking process, growth and profitability of the company.

Modest scale of lending operations with concentration of top 20 exposures

IIFL Wealth's lending operations remain modest with a loan book of ~Rs 2,500 crore as of H1FY21. Further, the portfolio is entirely concentrated on a single product, i.e. loans against securities to HNI clients with top 20 clients account for 48% of total loans.

Increasing competition from new Fintech players

The improvement in accessibility has resulted in many new players entering the wealth management field claiming to be technologically advanced and at lower fees. This could result in higher competition, impact the fees charged by the company and reduce profitability going forward.

Rise in attrition of RMs and TLs could impact growth in AUM

In wealth management business RMs and TLs play a big role in building and maintaining relationships with clients. In case there is a sharp rise in attrition of these, then it could impact the growth in AUM.

About the company

IIFL Wealth Management is one of the fastest growing private wealth management firms in India with an AUM greater than USD 27 billion. It serves the highly specialized and sophisticated needs of high net worth and ultra-high net worth individuals, affluent families, family offices and institutional clients through a comprehensive range of tailored wealth management solutions.

IIFL Wealth pioneered the concept of charging an advisory fee instead of commissions bringing transparency to all their dealings and inspiring clients' trust. The company offers wealth management and asset management services through its 31 offices across 6 countries.

IIFL Wealth Management Ltd.

Major business lines include:

- Discretionary and non-discretionary multi-asset-class PMS. “Discretionary” is managing investments where decisions to buy or sell are made at the portfolio manager's discretion. “Non-discretionary” is where clients instruct portfolio manager regarding which trades to execute
- Distribution of financial products across asset classes
- Solutions for debt, equity, real estate, commodities and currency
- Credit solutions
- Estate and succession planning

Wealth Management

IIFL Wealth Management is one of the leading wealth management companies in India and is the investment and financial advisor to more than 5,300 influential families in the High Net Worth Individuals (HNI) and Ultra HNI segments in India and abroad.

Asset Management

IIFL Asset Management is an India focused, global asset management firm providing products like mutual funds, portfolio management schemes and alternative investment funds that span across public and private equities as well as fixed income securities.

IIFL Wealth Management Ltd.

Financials

Income Statement

(Rs cr)	FY19	FY20	FY21P	FY22E	FY23E
Recurring Revenues	444	535	583	762	910
Non-Recurring Revenue	623	316	470	468	476
Total Income	**1067**	**851**	**1053**	**1231**	**1386**
Employee exp	331	373	409	448	488
Depreciation	22	41	43	49	51
Other exp	178	149	116	135	147
Total operating exp	531	563	568	632	686
PBT	**536**	**288**	**485**	**598**	**700**
Tax	163	85	116	150	175
PAT	**373**	**202**	**370**	**449**	**525**

Balance Sheet

(Rs cr)	FY19	FY20	FY21P	FY22E	FY23E
Share Capital	17	17	18	18	18
Reserves & Surplus	2893	2974	2810	2925	3054
Shareholder funds	**2910**	**2992**	**2828**	**2943**	**3072**
Borrowings	6103	8838	4712	4707	5177
Other Liab & Prov.	767	1191	1201	1071	1086
SOURCES OF FUNDS	**9780**	**13021**	**8740**	**8720**	**9335**
Fixed Assets	322	421	466	489	514
Investment	3053	6512	2513	2251	2118
Cash & Bank Balance	277	1179	788	655	659
Advances	4966	3632	3721	4093	4707
Other Assets	974	1088	879	859	965
TOTAL ASSETS	**9780**	**13021**	**8740**	**8720**	**9335**

Ratio Analysis

As at March (Rs cr)	FY19	FY20	FY21P	FY22E	FY23E
Return Ratios (%)					
Calc. Yield on ARR assets (%)	0.86	0.89	0.71	0.65	0.61
Calc. Yield on TBR assets	0.63	0.40	0.33	0.30	0.28
RoAE (excl. Goodwill)	16.3	7.3	14.1	17.9	19.9
RoAA	3.9	1.8	3.4	5.1	5.8
Growth Ratios (%)					
AUM	21.5	1.6	49.2	17.3	15.9
Total Income	2.3	-20.2	23.7	16.9	12.6
PAT	-22.0	-45.7	82.6	21.5	16.9
Per Share Data (Rs)					
EPS	44.1	23.2	42.0	51.1	59.7
Adj. BVPS	344.4	343.3	321.8	334.8	349.5
Dividend per share	10.0	20.0	70.0	38.0	45.0
Valuation Ratios (x)					
P/E	31.5	59.8	33.0	27.2	23.3
P/ABV	4.0	4.0	4.3	4.1	4.0
Dividend Yield (%)	0.7	1.4	5.0	2.7	3.2
Other Ratios (%)					
Cost-Income	49.7	66.2	53.9	51.4	49.5
Cost-Avg AUM	0.4	0.4	0.3	0.3	0.3

(Source: Company, HDFC sec Research)

IIFL Wealth Management Ltd.

Price chart

RETAIL RESEARCH

Disclosure:

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HDFC securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066

Compliance Officer: Binkle R. Oza Email: complianceofficer@hdfcsec.com Phone: (022) 3045 3600

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