

# CRISIL

## Ratings modest; currency woes dent research

India Equity Research | Credit Rating

CRISIL's 8.6% YoY revenue and 13.4% EBITDA growth in Q2CY17 came below estimates due to miss in research segment. Key highlights were: (1) research revenue growth slackened to 9% (14% in Q1CY17) impacted adversely by appreciating INR; (2) ratings revenue grew 5.7% YoY (4.3% in Q1CY17) led by large corporate ratings, whereas SME declined post reduction in NSIC subsidy; and (3) overall EBITDA margin expanded 107bps to 25.4% on account of downsizing in SME segment. Despite improving bond outlook, CRISIL is cautious on short-term credit growth and SME segment's prospects due to cut in NSIC subsidy. On account of expensive valuations maintain 'HOLD' using DCF with TP of INR2,068.

### Research: Currency woes hurt growth

Research revenue growth slowed to 9.2% YoY (14% in Q1CY17 and CY16) due to a much stronger INR during the quarter. Lower INR realisation also led to 3% YoY EBIT dip. While Financial research was muted, Risk & Analytics and Coalition continued to grow strongly. Risk & Analytics continued strong run led by model validation, stress testing & regulatory change management. Coalition could grow in double digits led by launch of new products. Further, the stress testing module is submitted to the government by March-April and revenues pick up in H2. Management has guided for 10% growth in the segment going forward.

### Ratings: Modest growth in subdued environment

Though ratings revenue growth was a modest 5.7% YoY, it was a pick up from 4.3% in Q1CY17. The spurt was driven by large corporate ratings, whereas SME fell post significant cut in NSIC subsidy. Domestic business environment improved, though private investments and credit off take remained weak due to low capacity utilisation and high leverage. CRISIL expects 8-12% growth in outsourced ratings in CY17. It estimates double digit growth in ratings in CY18 on improvement in private capex cycle and spurt in outsourced ratings. Due to cost control, particularly downsizing in SME segment as well as operating leverage, EBIT margin jumped 510bps, leading to EBIT rising 29%. It has guided for sustained margin improvement due to SME downsizing.

### Outlook and valuations: Short-term benign; maintain 'HOLD'

On account of expensive valuations we maintain 'HOLD' using DCF taking 15% growth for first 5 years, declining growth over the next 5 years to a terminal rate of 7% and discount rate of 10%. The stock is trading at 38.9x CY17E and 32.6x CY18E EPS.

Financials		(INR mn)						
Year to Dec.	Q2CY17	Q2CY16	Growth %	Q1CY17	Growth %	CY16	CY17E	CY18E
Revenue	4,073	3,750	8.6	4,022	1.3	15,472	16,934	19,228
EBITDA	1,034	911	13.4	1,106	(6.6)	4,615	5,046	5,903
Adjusted Profit	673	615	9.3	721	(6.8)	3,263	3,554	4,240
Adj. Dil. EPS (INR)	9.4	8.6	9.2	10.1	(6.9)	45.7	49.8	59.4
Diluted P/E (x)						42.3	38.9	32.6
EV/EBITDA (x)						28.6	26.0	22.1
ROAE (%)						36.2	35.4	37.6

#### EDELWEISS RATINGS

Absolute Rating	HOLD
Investment Characteristics	Growth
MARKET DATA (R: CRSL.BO, B: CRISIL IN)	
CMP	: INR 1,936
Target Price	: INR 2,086
52-week range (INR)	: 2,500 / 1,842
Share in issue (mn)	: 71.4
M cap (INR bn/USD mn)	: 138 / 2,149
Avg. Daily Vol. BSE/NSE ('000)	: 35.6

#### SHARE HOLDING PATTERN (%)

	Current	Q2FY17	Q1FY17
Promoters *	67.1	67.1	67.1
MF's, FI's & BKs	11.1	10.5	10.1
FII's	6.0	7.5	8.0
Others	15.9	14.9	14.8
* Promoters pledged shares (% of share in issue)	:		NIL

#### PRICE PERFORMANCE (%)

	BSE Midcap Index	Stock	Stock over Index
1 month	2.6	4.9	2.2
3 months	5.8	(2.2)	(8.0)
12 months	25.4	(6.8)	(32.2)

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**Table 1: Segment-wise performance**

	Q2CY17	Q2CY16	% YoY	Q1CY17	%QoQ	CY16	CY15	% YoY
<b>Segment revenue</b>								
Rating Services	1,163	1,100	5.7	1,146	1.4	4,676	4,341	7.7
Advisory Services	240	207	15.9	212	13.3	758	661	14.6
Research Services	2,662	2,438	9.2	2,656	0.3	10,038	8,797	14.1
<b>Total</b>	<b>4,065</b>	<b>3,745</b>		<b>4,014</b>		<b>15,472</b>	<b>13,799</b>	
<b>Segment EBIT</b>								
Rating Services	325	251	29.3	303	7.2	1481	1,471	0.7
Advisory Services	28	-8	(472.4)	4	NA	14	23	(38.5)
Research Services	715	737	(3.0)	830	(13.8)	3312	2,740	20.9
<b>Total</b>	<b>1,068</b>	<b>980</b>		<b>1136</b>		<b>4807</b>	<b>4,233</b>	
<b>Segment EBIT margin (%)</b>								
Rating Services	27.9	22.8	5.1	26.4	1.5	31.7	33.9	(2.2)
Advisory Services	11.8	(3.7)	15.4	1.7	10.1	1.9	3.5	(1.6)
Research Services	26.9	30.2	(3.4)	31.2	(4.4)	33.0	31.1	1.9

Source: Company, Edelweiss research

## Other highlights

- **Dividend:** During the quarter, CRISIL declared interim dividend of INR6/share.
- CRISIL reported forex loss of INR21.2mn in Q2CY17 (as part of other expenses) versus gain of INR47.1mn in Q2CY16 on account of a strengthening INR.
- IND-AS was applicable to the company from January 1, 2017. All quarterly numbers have been restated as per IND-AS.

## Operations highlights

- **Research revenue grew 9.2%** led by addition of clients in India Research and Global Research & Analytics. The slowdown (growth of 14% in Q1CY17 and CY16) in research was impacted by lower realisations due to appreciating INR, which also led to margin dip. Adverse forex movement, slow financial research as well as a seasonally slow Q2 led to slower growth in research. Risk & Analytics continued to grow strongly led by model validation, stress testing, regulatory change management and financial crime and compliance analytics. Coalition delivered good growth through its core products and commercialisation of Transaction Banking and Securities Services analytics and it is expected to continue to grow in double digits. In India, 'Quantix' was launched, a data analytics platform that leverages CRISIL's large data repository. Management has guided H2CY17 to be stronger for the segment and going forward it expects to grow at 8-10% in constant currency.
- **Ratings revenue grew 5.7% YoY** on a weak base (growth of 1.4% in Q2CY16) due to continued weak investment climate and soft credit growth. Growth was driven by robust spurt in large corporate ratings, while SME segment declined due to significant cut in government subsidy. Overall domestic environment has improved, though private investments and credit off take remain weak on account of low capacity utilisation and high leverage. Outsourced S&P ratings continued to grow steadily at 8-12%. Management stated that the outlook is dependent on private capex cycle, which could improve from CY18, which could lead to double digit growth. Margin expanded

on account of cost control, particularly downsizing in SME segment as well as operating leverage. Healthy margins are expected to sustain.

- **Advisory revenue grew a strong 16% YoY** during the quarter. CRISIL has built a healthy order book and will continue to garner a healthy pipeline.

### Financial snapshot

(INR mn)

Year to December	Q2CY17	Q2CY16	% change	Q1CY17	% change	YTD17	CY17E	CY18E
Net revenues	4,073	3,750	8.6	4,022	1.3	8,095	16,934	19,228
Staff costs	2,137	2,032	5.2	1,980	8.0	4,117	8,366	9,364
Other expenses	902	806	11.9	936	(3.7)	1,839	3,522	3,961
Total expenditure	3,040	2,838	7.1	2,916	4.2	5,955	11,888	13,325
EBITDA	1,034	911	13.4	1,106	(6.6)	2,140	5,046	5,903
Depreciation	127	139	(8.4)	129	(0.9)	256	413	447
EBIT	906	772	17.3	978	(7.3)	1,884	4,634	5,457
Other income	85	127	(33.0)	70	21.1	155	444	600
Interest								
Add: Prior period items								
Add: Exceptional items								
Profit before tax	991	899	10.2	1,048	(5.4)	2,039	5,078	6,057
Provision for taxes	319	284	12.2	327	(2.4)	645	1,523	1,817
Associate profit share								
Profit- Discontinued Ops								
Reported net profit	673	615	9.3	721	(6.8)	1,394	3,554	4,240
Adjusted Profit	673	615	9.3	721	(6.8)	1,394	3,554	4,240
Diluted shares (mn)	71	71		71		143	71	71
Adjusted Diluted EPS	9.4	8.6	9.2	10.1	(6.9)	19.5	49.8	59.4
Diluted P/E (x)	-	-		-		-	38.9	32.6
EV/EBITDA (x)	-	-		-		-	26.0	22.1
ROAE (%)	-	-		-		-	35.4	37.6
Market cap / rev. (x)	-	-		-		-	8.2	7.2
<b>As % of net revenues</b>								
Employee cost	52.5	54.2		49.2		101.7	49.4	48.7
Other expenses	22.1	21.5		23.3		45.4	20.8	20.6
EBITDA	25.4	24.3		27.5		52.9	29.8	30.7
Reported net profit	16.5	16.4		17.9		34.4	21.0	22.0

## Company Description

CRISIL is India's leading credit rating, research, risk & policy advisory company having pioneered the concept of credit rating in India in 1987. S&P, the world's leading credit rating agency by market share, is its major shareholder (67.7%) after the recent open offer.

CRISIL is a globally diversified analytical company having ratings, research and advisory services under its fold. With market leadership in corporate bonds, bank loan ratings and SME ratings, company is strongly poised to gain from cyclical and structural uptick in domestic ratings segment. With increased interest from parent, strong growth in off shoring services to S&P will continue which will drive its offshore ratings segment (Global Analytic Center). Being a global research analytics company providing off shoring services to several large global clients like 12 of top 15 global investment banks, two of the top 10 global consulting groups, three of the top 15 global insurance companies and 37 Fortune 500 companies, company is expected to continue its strong momentum in research revenues.

## Investment Theme

CRISIL is India's leading credit rating company having a ~35% revenue market share, and a strong parentage—Standard & Poor (S&P), world's leading credit rating agency by market share. Based on recovery in the Indian economy and increased penetration of debt market in India, we are factoring in 8% CAGR in ratings sales over CY16-18E. Also, we have assumed 12% CAGR in research revenue over CY16-18E.

## Key Risks

### Adverse macro economy

Ratings agencies are vulnerable to downturns in the economy when capital raising activities fall. Last year, fund raising activities dipped due to weakness in the economy and corporate level stress, which in turn led to reduced bond issuances and bonds rating businesses. Also with ~65% consolidated revenue from outside India and 29% revenue being Europe linked, the company's overall revenue could face some pressure.

### Migration to internal ratings based approach by banks

If banks whose clients avail credit rating services under the Basel II framework migrate to the internal rating based approach for credit risk (the IRB Approach), it could have an adverse effect on CRISIL's rating business.

### Pricing transience to fixed fee structure

Limited bond issuance and lower bank loan rating volumes pose a threat as issuances have transcended to a fixed fee cap structure. However, this is more so pronounced only in the BLR market and less in the CDR segment which is more profitable.

### Risk of defaults

Any rating default by a client would hamper the credibility of the rating agency. However SEBI's mandatory disclosures of default rates would keep the rating agency under control of the watch guard.

## Financial Statements

### Key Assumptions

Year to December	CY15	CY16	CY17E	CY18E
<b>Macro</b>				
GDP(Y-o-Y %)	7.2	6.5	7.1	7.7
Inflation (Avg)	4.9	4.5	4.0	4.5
Repo rate (exit rate)	6.8	6.3	5.8	5.8
USD/INR (Avg)	65.0	67.5	66.0	66.0
<b>Sector</b>				
Corp debt iss. growth(%)	17.0	20.0	13.0	16.0
Banking cr. growth (%)	14.0	15.0	16.0	18.0
<b>Company</b>				
Vol of debt rated(INRbn)	5,741	6,783	7,545	8,752
Number of new assignments	3,312	2,741	2,881	3,169
Nos	16,000	18,000	15,840	17,107
Rating revenues (INR mn)	4,342	4,637	4,916	5,486
Domestic Ratings	2,873	3,061	3,183	3,544
CDR inc(INR mn)	1,389	1,594	1,773	2,057
BLR inc(INR mn)	924	868	909	963
SME	561	599	501	525
S&P Ratings	1,468	1,576	1,733	1,941
Advisory services	661	758	894	1,055
Research revenue(INR mn)	6,430	7,443	8,219	9,346
Irevna	6,967	8,012	8,813	9,959
Pipal Research	265	273	289	315
India Research	(801)	(841)	(883)	(928)
Coalition Development	2,367	2,594	2,906	3,341
Total Revenues (INR mn)	11,433	12,838	14,029	15,887
Rating revenues (%)	38.0	36.1	35.0	34.5
Domestic Ratings	25.1	23.8	22.7	22.3
S&P Ratings	12.8	12.3	12.4	12.2
Advisory services	5.8	5.9	6.4	6.6
Research revenues (%)	56.2	58.0	58.6	58.8
Irevna	60.9	62.4	62.8	62.7
Pipal Research	2.3	2.1	2.1	2.0
India Research	(7.0)	(6.6)	(6.3)	(5.8)
Coalition Development	20.7	20.2	20.7	21.0

### Income statement

(INR mn)

Year to December	CY15	CY16	CY17E	CY18E
Net revenue	13,799	15,472	16,934	19,228
Gross profit	6,860	7,722	8,569	9,864
Employee costs	6,939	7,749	8,366	9,364
Other Expenses	2,864	3,107	3,522	3,961
EBITDA	3,996	4,615	5,046	5,903
Depreciation	371	404	413	447
EBIT	3,625	4,212	4,634	5,457
Add: Other income	432.23	547.13	444.13	600.05
Profit Before Tax	4,057	4,759	5,078	6,057
Less: Provision for Tax	1,205	1,495	1,523	1,817
Reported Profit	2,852	3,263	3,554	4,240
Adjusted Profit	2,852	3,263	3,554	4,240
Shares o/s (mn)	71	71	71	71
Adjusted Basic EPS	40.0	45.7	49.8	59.4
Diluted shares o/s (mn)	71	71	71	71
Adjusted Diluted EPS	40.0	45.7	49.8	59.4
Adjusted Cash EPS	44.4	51.1	55.6	65.7
Dividend per share (DPS)	23.0	27.0	29.0	35.0
Dividend Payout Ratio(%)	69.2	71.0	67.5	68.3

### Common size metrics

Year to December	CY15	CY16	CY17E	CY18E
Operating expenses	71.0	70.2	70.2	69.3
Depreciation	2.7	2.6	2.4	2.3
EBITDA margins	29.0	29.8	29.8	30.7
Net Profit margins	20.7	21.1	21.0	22.0

### Growth ratios (%)

Year to December	CY15	CY16	CY17E	CY18E
Revenues	10.1	12.1	9.5	13.5
EBITDA	2.9	15.5	9.3	17.0
PBT	7.9	17.3	6.7	19.3
Adjusted Profit	6.2	14.4	8.9	19.3
EPS	6.5	14.2	8.9	19.3

Balance sheet		(INR mn)			
As on 31st December	CY15	CY16	CY17E	CY18E	
Share capital	71	71	71	71	
Reserves & Surplus	8,486	9,382	10,537	11,880	
Shareholders' funds	8,558	9,454	10,608	11,952	
Long Term Liabilities	325	236	236	102	
Def. Tax Liability (net)	(363)	(385)	(385)	(385)	
<b>Sources of funds</b>	<b>8,520</b>	<b>9,304</b>	<b>10,459</b>	<b>11,669</b>	
Gross Block	6,084	5,871	6,271	6,671	
Net Block	785	664	652	605	
Capital work in progress	26	42	42	42	
Intangible Assets	3,341	3,037	3,037	3,037	
Total Fixed Assets	4,152	3,743	3,730	3,684	
Non current investments	56	56	56	56	
Cash and Equivalents	5,295	6,014	6,936	7,953	
Sundry Debtors	1,956	2,101	2,320	2,739	
Loans & Advances	890	1,078	1,078	1,078	
Other Current Assets	597	985	985	985	
Current Assets (ex cash)	3,443	4,164	4,383	4,803	
Trade payable	354	416	390	436	
Other Current Liab	4,072	4,257	4,257	4,391	
Total Current Liab	4,426	4,673	4,647	4,827	
Net Curr Assets-ex cash	(983)	(509)	(264)	(24)	
<b>Uses of funds</b>	<b>8,520</b>	<b>9,304</b>	<b>10,459</b>	<b>11,669</b>	
BVPS (INR)	120.2	132.5	148.7	167.5	

Free cash flow		(INR mn)			
Year to December	CY15	CY16	CY17E	CY18E	
Reported Profit	2,852	3,263	3,554	4,240	
Add: Depreciation	371	404	413	447	
Others	(722)	(1,277)	(491)	(746)	
Less: Changes in WC	(203)	(400)	(246)	(373)	
Operating cash flow	2,704	2,789	3,722	4,313	
Less: Capex	262	233	400	400	
<b>Free Cash Flow</b>	<b>2,442</b>	<b>2,556</b>	<b>3,322</b>	<b>3,913</b>	

## Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		P/B (X)		ROAE (%)	
		CY17E	CY18E	CY17E	CY18E	CY17E	CY18E
Crisil	2,149	38.9	32.6	13.0	11.6	35.4	37.6
CARE Ratings Limited	750	31.2	27.4	8.9	8.1	29.8	31.0
ICRA	613	45.2	36.2	7.2	6.5	16.7	18.8
Median	-	38.9	32.6	8.9	8.1	29.8	31.0
AVERAGE	-	38.4	32.0	9.7	8.7	27.3	29.1

Source: Edelweiss research

Cash flow metrics					
Year to December	CY15	CY16	CY17E	CY18E	
Operating cash flow	2,704	2,789	3,722	4,313	
Investing cash flow	9	(247)	(400)	(400)	
Financing cash flow	(2,608)	(2,213)	(2,400)	(2,896)	
Net cash Flow	104	330	922	1,017	
Capex	(262)	(233)	(400)	(400)	
Dividend paid	(1,973)	(2,402)	(2,400)	(2,896)	

## Profitability and efficiency ratios

Year to December	CY15	CY16	CY17E	CY18E
ROAE (%)	33.5	36.2	35.4	37.6
ROACE (%)	47.6	52.8	50.6	53.7
ROA	33.5	36.6	36.0	38.3
Debtors Days	44	48	48	48
Payable Days	19	20	21	23
Cash Conversion Cycle	25	30	30	32
Debt / Cap employed (%)	47.7	46.1	40.7	38.1

## Operating ratios

Year to December	CY15	CY16	CY17E	CY18E
Total Asset Turnover	1.6	1.7	1.7	1.7
Fixed Asset Turnover	3.3	4.0	4.6	5.2
Equity Turnover	1.6	1.7	1.7	1.7

## Valuation parameters

Year to December	CY15	CY16	CY17E	CY18E
Adj. Diluted EPS (INR)	40.0	45.7	49.8	59.4
Y-o-Y growth (%)	6.5	14.2	8.9	19.3
Adjusted Cash EPS (INR)	44.4	51.1	55.6	65.7
Diluted P/E (x)	48.4	42.3	38.9	32.6
P/B (x)	16.1	14.6	13.0	11.6
EV / Sales (x)	9.6	8.5	7.7	6.8
EV / EBITDA (x)	33.2	28.6	26.0	22.1
Dividend Yield (%)	1.2	1.4	1.5	1.8

### Additional Data

#### Directors Data

Mr. Douglas L. Peterson	Chairman	Ms. Ashu Suyash	Managing Director and Chief Executive Officer
Mr. Ravinder Singhanian	Alternate Director to Douglas Peterson	Mr. H.N. Sinor	Director
Dr. Nachiket Mor	Director	Mr. M. Damodaran	Director
Ms. Vinita Bali	Director	Ms. Martina L. Cheung	Director
Mr. John L. Berisford	Director		

Auditors - S. R. Batliboi & Co

*\*as per last available data*

#### Holding Top -10

	Perc. Holding		Perc. Holding
General Insurance Corp of India	3.78	UTI Asset Management	0.53
Matthews Intl Capital	2.51	ICICI Prudential Asset Management	0.38
Life Insurance Corporation of India	2.06	Blackrock	0.37
Unit Trust of India	1.64	Birla Sunlife Asset Management	0.28
Sundaram Asset Management	0.62	Dimensional Fund Advisors	0.26

*\*as per last available data*

#### Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
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No Data Available

*\*as per last available data*

#### Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
21 Sep 2016	Gurpreet Chhatwal	Sell	19649.00

*\*as per last available data*



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### Coverage group(s) of stocks by primary analyst(s): Credit Rating

CARE Ratings Limited, Crisil, ICRA

#### Recent Research

Date	Company	Title	Price (INR)	Recos
17-May-17	CARE	Muted quarter; outlook positive; <i>Result Update</i>	1,536	Buy
15-May-17	ICRA	Focus on core to facilitate margin expansion; <i>Result Update</i>	4,199	Hold
24-Apr-17	Crisil	Subdued performance further dented by external factors; <i>Result Update</i>	1,912	Hold

#### Distribution of Ratings / Market Cap

##### Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

#### Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

#### One year price chart



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