

# Indostar Capital Finance

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Bloomberg	INDOSTAR IN
Equity Shares (m)	123.2
M.Cap.(INRb)/(USDb)	31.2 / 0.4
52-Week Range (INR)	298 / 166
1, 6, 12 Rel. Per (%)	-12/-3/-16
12M Avg Val (INR M)	44

## Financials & Valuations (INR b)

Y/E March	2020	2021E	2022E
NII	6.0	5.6	6.2
PPP	3.8	3.6	4.1
PAT	-3.2	1.2	1.7
EPS (INR)	-35.1	13.2	18.6
EPS Gr. (%)	NA	NA	41
BV (INR)	290	305	324

## Ratios

NIM (%)	6.6	6.9	7.0
C/I ratio (%)	47.8	46.7	45.2
RoA (%)	-3.0	1.2	1.6
RoE (%)	-11.4	4.4	5.9
Payout (%)	0.0	0.0	0.0

## Valuations

P/E (x)	-7.2	19.3	13.6
P/BV (x)	0.9	0.8	0.8
Div. Yield (%)	0.0	0.0	0.0

## Shareholding pattern (%)

As On	Jun-20	Mar-20	Jun-19
Promoter	45.5	60.6	60.7
DII	2.4	17.2	11.8
FII	0.0	5.8	9.8
Others	52.1	16.3	17.7

FII Includes depository receipts

**CMP: INR254**
**TP: INR290 (+14%)**
**Neutral**

## Moratorium rate down to 59% from 90%

- **Indostar Capital Finance (INDOSTAR) reported 1QFY21 PAT of INR472m v/s net loss of INR4.2b in the prior quarter.** The quarter was characterized by a stable loan book, healthy PPOp, and modest credit costs.
- **During the quarter, Brookfield infused INR12.25b capital via preferential allotment and CCPS. Moreover, by the start of July, it had also completed the open offer. As a result, Brookfield now owns 54% of the company, which shall further increase to 57% post the CCPS conversion.**

## Loan book stable; 25%+ liquidity on the balance sheet

- AUM was largely stable sequentially at INR100b, with the share of retail lending at 70%. **Within corporate lending, the share of non-real estate finance declined to a multi-quarter low of 16%.**
- While spreads were largely stable YoY at 4%, cost of funds remains elevated at 10.4%. During the quarter, the company raised INR7.3b in fresh borrowings via banks and market borrowings. **INDOSTAR now has INR18b liquidity on the balance sheet, amounting to 25%+ of borrowings.**

## Moratorium book down to 59% from 90%

- The key improvement in moratorium rate was driven by the retail lending book; the rate stood at 44% as of 31<sup>st</sup> July. **Within the retail lending book, the moratorium rate was as follows – CV: 42%, SME: 58%, and Housing: 25%. However, in the corporate lending book, the moratorium rate remains elevated at 90%.**
- Marginal improvement was seen in 1dpd+ in the Retail Lending segment from May to June – **CV: 44% to 38%; SME: 15% to 11%; Housing: 1.9% to 1.5%.** Also, retail collection efficiency was at 50% of pre-COVID-19 levels in July.

## Other highlights

- **The company continues to rationalize its branch network, which is down from 322 branches to 212 branches YoY.**
- In the Corporate Lending business, yield declined 70bp QoQ to 13.6%.
- The GNPL/NNPL ratio was largely stable at 4.4%/3.5%.
- **Post the deal with Brookfield, networth increased to INR40b from INR27b, and CRAR increased to 38% QoQ from 25%.**
- It has INR7.2b vehicle finance AUM under the ICICI Bank partnership.

## Key concall highlights

- **ECL provisions** – These were as follows: Stage 1: more than 0.4%; Stage 2: 6–8%; and Stage 3: 27% in CV, 20% in HFC, and 20–22% in SME. INDOSTAR has INR2.8b COVID-19 provisions over and above this.
- Incremental funding is at 8.5–9.5%.

## Valuation and view

INDOSTAR's plan to diversify its loan book has faced headwinds in the tough liquidity environment. On the asset quality front, two large corporate accounts that were stressed have been written off and are out of the books. The key concern pertains to asset quality trends post the lifting of the moratorium, especially since its moratorium rate is higher than that of most peers. While the company is very well-capitalized with a strong new parent, we expect modest growth over the next 12–18 months. Hence, RoE is likely to remain only in the mid-to-high single digits. Maintain Neutral, with TP of INR290 (0.9x FY22E BVPS).

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**Investors are advised to refer through important disclosures made at the last page of the Research Report.**

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Quarterly performance									(INR m)	
Y/E March	FY20				FY21				FY20	FY21
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q		
Interest Income	3,817	3,718	3,391	3,040	3,076	3,138	3,201	3,221	13,966	12,636
Interest Expenses	2,260	2,049	1,808	1,822	1,732	1,749	1,784	1,792	7,938	7,058
<b>Net Interest Income</b>	<b>1,557</b>	<b>1,670</b>	<b>1,584</b>	<b>1,217</b>	<b>1,344</b>	<b>1,389</b>	<b>1,416</b>	<b>1,429</b>	<b>6,028</b>	<b>5,578</b>
YoY Growth (%)	39.7	20.8	12.2	-4.0	-13.6	-16.8	-10.6	17.4	16.4	-7.5
Other Income	374	521	267	166	146	215	310	426	1,328	1,098
<b>Total Income</b>	<b>1,931</b>	<b>2,190</b>	<b>1,850</b>	<b>1,384</b>	<b>1,491</b>	<b>1,604</b>	<b>1,726</b>	<b>1,855</b>	<b>7,355</b>	<b>6,676</b>
YoY Growth (%)	70.5	22.1	7.4	-21.9	-22.8	-26.8	-6.7	34.1	14.6	-9.2
Operating Expenses	738	793	741	1,247	753	774	799	791	3,518	3,117
<b>Operating Profit</b>	<b>1,193</b>	<b>1,397</b>	<b>1,110</b>	<b>137</b>	<b>737</b>	<b>829</b>	<b>927</b>	<b>1,065</b>	<b>3,837</b>	<b>3,558</b>
YoY Growth (%)	101.7	26.8	-2.9	-87.7	-38.2	-40.7	-16.5	676.1	-3.0	-7.3
Provisions & Loan Losses	608	722	1,107	5,767	232	500	700	601	8,204	2,034
<b>Profit before Tax</b>	<b>585</b>	<b>675</b>	<b>3</b>	<b>-5,629</b>	<b>505</b>	<b>329</b>	<b>227</b>	<b>463</b>	<b>-4,367</b>	<b>1,525</b>
Tax Provisions	114	181	0	-1,416	33	86	59	127	-1,121	305
<b>Net Profit</b>	<b>471</b>	<b>494</b>	<b>2</b>	<b>-4,214</b>	<b>472</b>	<b>244</b>	<b>168</b>	<b>336</b>	<b>-3,246</b>	<b>1,220</b>
YoY Growth (%)	49.6	-22.8	-99.7	-668.8	0.2	-50.7	6,901.3	-108.0	-234.8	-137.6
<b>Key Operating Parameters (%)</b>										
Yield on loans (Cal)	15.0	15.5	15.5	15.0	15.6				15.1	
Cost of funds (Cal)	10.6	10.4	10.3	11.2	10.2				10.2	
Spreads (Cal)	4.4	5.0	5.2	3.8	5.4				4.9	
NIMs (Reported)	6.7	8.0	7.4	6.2	6.1					
Credit Cost	2.1	2.6	4.2	22.8	0.9				7.6	
Cost to Income Ratio	38.2	36.2	40.0	90.1	50.5				47.8	
Tax Rate	19.4	26.8	11.1	25.1	6.6				25.7	
<b>Balance Sheet Parameters</b>										
AUM (INR B)	115.8	107.2	102.2	99.7	100.9				78.0	
Change YoY (%)	55.0	38.0	31.9	-15.1	-12.9				-24.7	
AUM Mix (%)										
Vehicle	40.9	42.2	43.9	45.3	45.4				45.3	
Housing	5.5	6.6	7.5	8.3	8.2				8.3	
SME & Others	16.4	17.4	17.6	17.5	17.4				17.5	
Corporate	37.2	33.8	31.0	28.8	29.0				28.8	
Disbursements (INR B)	12.4	6.6	8.8	7.3	0.9				37.3	
Change YoY (%)	-45.1	-49.3	2.6	-63.9	-93.0				-42.1	
Borrowings (INR B)	81	76	64	67	72				66.8	
Change YoY (%)	51.6	31.4	2.0	-25.2	-11.5				-25.2	
Borrowings Mix (%)										
Banks	45	49	55	52	50					
NCDs	36	30	36	31	32					
CPs	3	3	0	0	1					
Others	16	18	9	17	16					
Debt/Equity (x)	2.6	2.5	2.1	2.5	1.8				2.5	
<b>Asset Quality Parameters (%)</b>										
GS 3 (INR B)	4.9	3.4	3.8	3.7	3.8				3.7	
Gross Stage 3 (% on Assets)	4.7	3.7	4.4	4.5	4.4				4.6	
NS 3 (INR B)	3.8	2.8	3.0	2.9	3.0				2.9	
Net Stage 3 (% on Assets)	3.7	3.0	3.5	3.6	3.5				3.7	
PCR (%)	22.1	19.5	21.0	20.8	20.9				20.8	
<b>Return Ratios (%)</b>										
ROA (Rep)	1.6	1.8	0	-18.3	1.9				-3.0	
ROE (Rep)	6.2	6.4	0	-58.4	5.7				-11.4	

Source: Company, MOFSL



## Highlights from management commentary

### Business updates

- The focus is on opex reduction (salary and rent, among others).
- Expect to disburse loans worth INR4–5b under ECLGS.
- It has undertaken certain projects on the digitization front. The quantum of these expenses was INR100m in 1QFY21.
- Some part of the AUM growth was attributable to interest capitalization.

### Asset quality / Moratorium

- Morat 2.0 was an opt-in rather than an opt-out.
- Corporate NPL comprises just one account that turned NPL in 1QFY20. It holds 10% provisions against this asset and is confident of recovery in the asset.
- **ECL provisions – These were as follows: Stage 1: more than 0.4%; Stage 2: 6–8%; and Stage 3: 27% in CV, 20% in HFC, and 20–22% in SME. INDOSTAR has INR2.8b COVID-19 provisions over and above this.**
- More stress in new CV financing v/s used CV financing, primarily in central and northern India.
- **It plans to consider moratorium for wholesale lending on a case-by-case basis. In retail lending, it would reach 20–25% moratorium in August. It would reach 90% collection efficiency in retail in September or October.**

### Liquidity/Funding

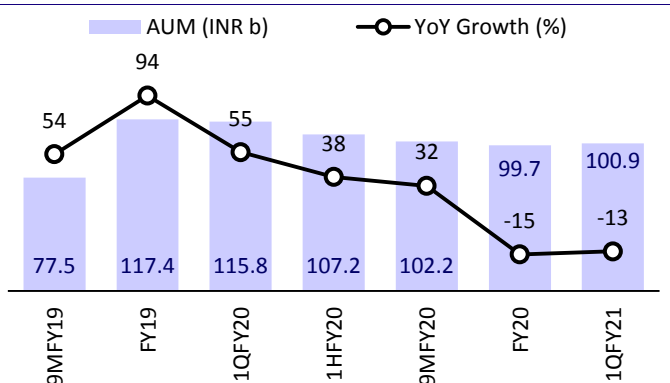
- **Incremental funding is at 8.5–9.5% (one loan came in at sub-6%).**
- It has raised INR9.76b since April 1.

### Others

- Do not expect branch expansion in the near term.
- Collection efficiency numbers include arrear collections. Excluding these, numbers would be 4–5% lower.
- A typical SME customer is a business with turnover up to INR100m. ATS is at INR10m. Some loans have been assigned in this segment.
- Non-morat customers are those who have paid at least one EMI.
- Low tax rate this quarter is due to a change in the policy of calculation of deferred tax rate.
- Most of the real estate lending is seen in the Affordable segment. It is confident of cash flow covers in this book.
- INR2.07b write-offs were reported in the Corporate portfolio and INR600m in the Vehicle Finance portfolio in 4QFY20.

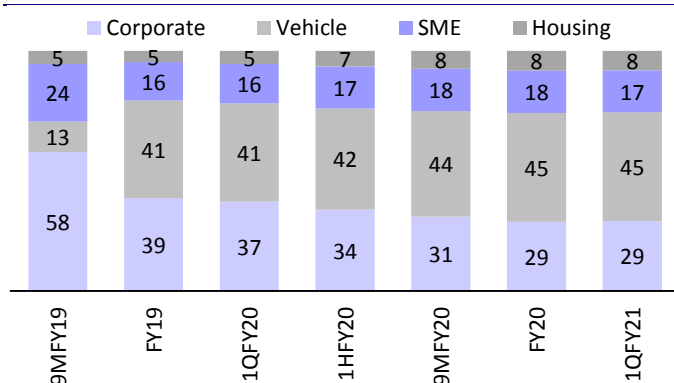
## Key exhibits

**Exhibit 1: Loan book now stable**



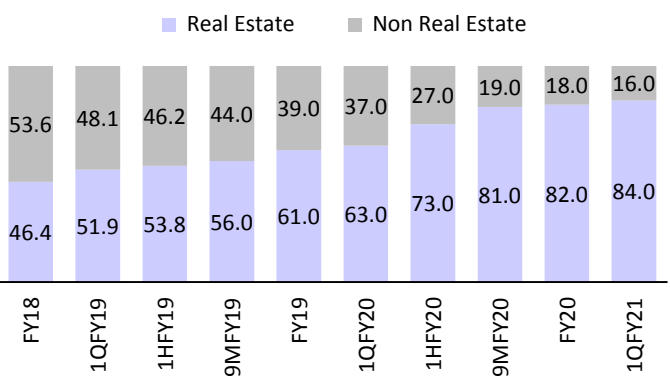
Source: MOFSL, Company; Note: Acquired IIFL CV business in 4QFY19

**Exhibit 2: Trend in AUM mix (%)**



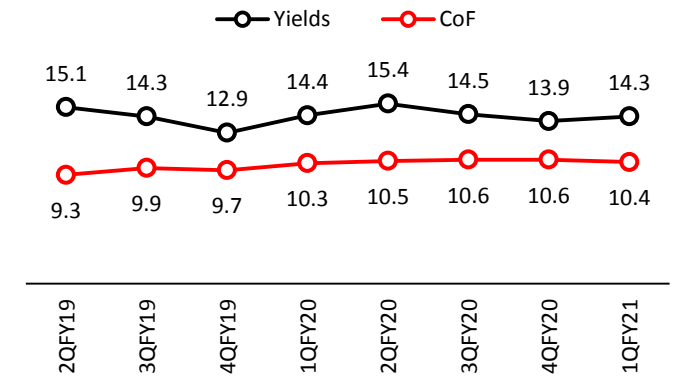
Source: MOFSL, Company

**Exhibit 3: Share of non-RE declining (%)**



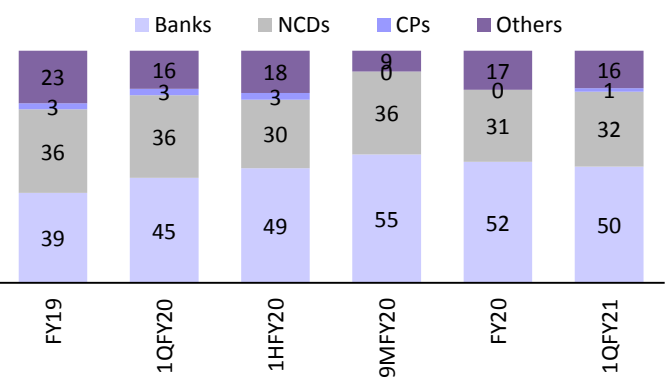
Source: MOFSL, Company

**Exhibit 4: Spreads have been stable (%)**



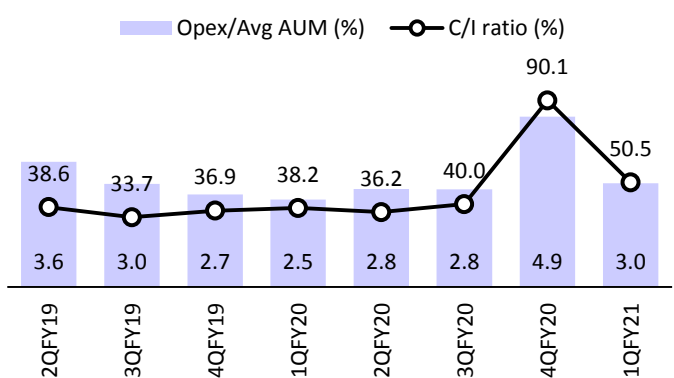
Source: MOFSL, Company; Note: 4QFY19 numbers are an anomaly due to acq. of IIFL business on the last day of the qtr

**Exhibit 5: Trend in borrowing mix (%)**



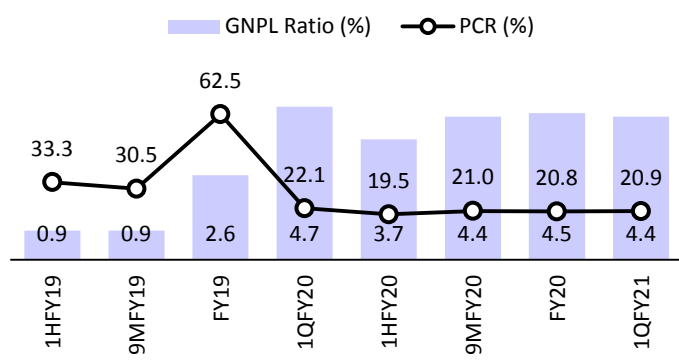
Source: MOFSL, Company

**Exhibit 6: Expense ratio at run-rate levels**



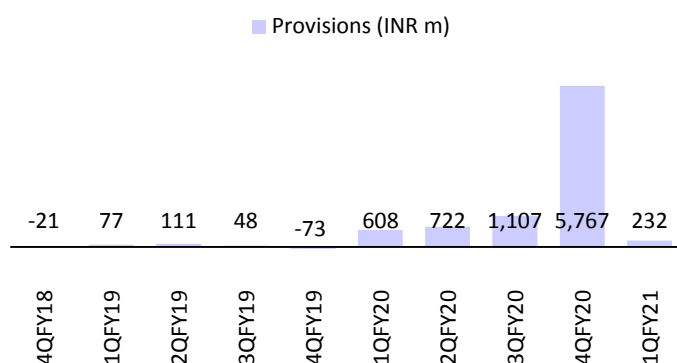
Source: MOFSL, Company; One-off accounting adjustment in 4QFY20

**Exhibit 7: Asset quality stable**



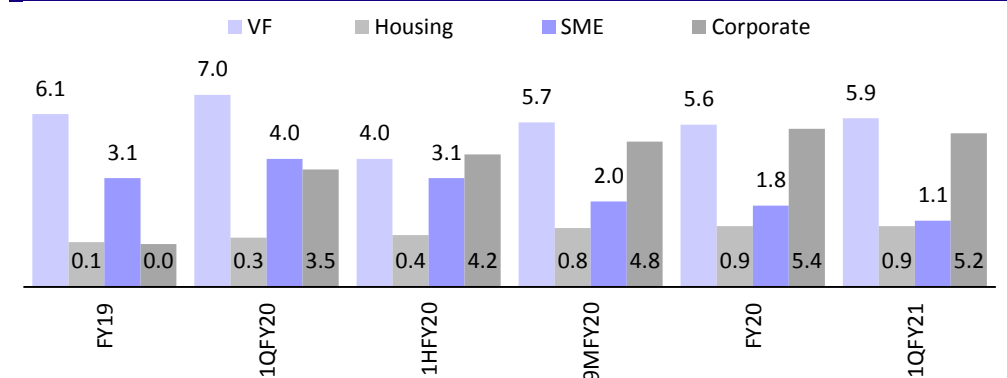
Source: MOFSL, Company

**Exhibit 8: Credit costs back to normal**



Source: MOFSL, Company

**Exhibit 9: Stable asset quality across product segments (%)**



Source: MOFSL, Company

### Valuation and view

- INDOSTAR’s plans to diversify its loan book have faced headwinds given the tough liquidity environment. Disbursements have been calibrated, while cost of funds remains elevated.
- Management has tried to resolve this by entering into a co-lending arrangement with ICICI Bank. It is also in talks with other banks for SME lending. While these are positive steps, we would wait and see how it progresses. However, traction from the acquired erstwhile IIFL business also remains slow.
- On the asset quality front, two large corporate accounts that were stressed have been written off and are out of the books. The key concern pertains to asset quality trends post the lifting of the moratorium, especially since its moratorium rate is higher than that of most peers.
- While the company is very well-capitalized with a strong new parent, we expect modest growth over the next 12–18 months. Hence, RoE is likely to remain only in the mid-to-high single digits. Maintain Neutral, with TP of INR290 (0.9x FY22E BVPS).

**Exhibit 10: Valuation Matrix**

	Rating	CMP (INR)	Mcap (USD b)	P/E (x)		P/BV (x)		RoA (%)		RoE (%)	
				FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
<b>HFCs</b>											
LICHF	Buy	271	1.8	6.4	5.6	0.7	0.6	1.0	1.1	11.5	11.8
PNBHF	Neutral	230	0.5	5.2	3.8	0.5	0.4	1.0	1.3	9.1	11.3
<b>Vehicle fin.</b>											
SHTF	Buy	703	2.0	10.4	6.1	0.8	0.8	1.5	2.6	8.7	13.0
MMFS	Buy	134	1.1	18.2	15.0	1.1	1.0	1.2	1.5	6.8	7.0
CIFC	Buy	225	2.3	15.7	11.4	2.0	1.8	1.8	2.2	13.8	16.6
<b>Diversified</b>											
BAF	Neutral	3,419	27.4	46.3	28.3	5.6	4.8	2.5	3.6	12.9	18.3
SCUF	Buy	717	0.6	6.2	5.2	0.6	0.5	2.5	3.0	10.0	11.0
LTFH	Buy	66	1.7	13.3	6.9	0.9	0.8	0.9	1.7	6.7	12.0
MUTH	Neutral	1,177	6.2	13.1	11.5	3.3	2.7	6.7	6.7	27.7	25.6
MAS	Buy	661	0.5	21.4	17.9	3.2	2.8	3.7	4.0	16.0	16.9

## Financials and valuations

Income Statement								(INR m)
Y/E March	2016	2017	2018	2019	2020	2021E	2022E	2023E
Interest Income	5,644	6,436	7,631	10,813	13,966	12,636	13,610	15,262
Interest Expended	2,893	3,118	3,256	5,636	7,938	7,058	7,400	8,070
<b>Net Interest Income</b>	<b>2,751</b>	<b>3,317</b>	<b>4,376</b>	<b>5,177</b>	<b>6,028</b>	<b>5,578</b>	<b>6,210</b>	<b>7,193</b>
Change (%)	31.8	20.6	31.9	18.3	16.4	-7.5	11.3	15.8
Fee Income	796	756	258	1,244	1,328	1,098	1,281	1,473
<b>Net Income</b>	<b>3,548</b>	<b>4,081</b>	<b>4,634</b>	<b>6,420</b>	<b>7,355</b>	<b>6,676</b>	<b>7,491</b>	<b>8,666</b>
Change (%)	31.3	15.0	13.6	38.5	14.6	-9.2	12.2	15.7
Operating Expenses	582	727	1,547	2,466	3,518	3,117	3,389	3,789
<b>Operating Income</b>	<b>2,966</b>	<b>3,354</b>	<b>3,087</b>	<b>3,954</b>	<b>3,837</b>	<b>3,558</b>	<b>4,102</b>	<b>4,877</b>
Change (%)	29.5	13.1	-8.0	28.1	-3.0	-7.3	15.3	18.9
Provisions and W/Offs	34	123	-38	163	8,204	2,034	1,801	1,532
<b>PBT</b>	<b>2,932</b>	<b>3,230</b>	<b>3,125</b>	<b>3,792</b>	<b>-4,367</b>	<b>1,525</b>	<b>2,301</b>	<b>3,344</b>
Tax	1,016	1,122	1,122	1,384	-1,121	305	580	843
Tax Rate (%)	34.6	34.7	35.9	36.5	25.7	20.0	25.2	25.2
<b>PAT</b>	<b>1,916</b>	<b>2,108</b>	<b>2,003</b>	<b>2,408</b>	<b>-3,246</b>	<b>1,220</b>	<b>1,721</b>	<b>2,502</b>
Change (%)	28.6	10.0	-5.0	20.2	-234.8	-137.6	41.1	45.4

Balance Sheet								(INR m)
Y/E March	2016	2017	2018	2019	2020	2021E	2022E	2023E
Equity Share Capital	734	784	787	923	925	925	925	925
Reserves & Surplus	14,684	18,084	19,961	29,140	25,881	27,291	29,012	31,513
<b>Net Worth</b>	<b>15,418</b>	<b>18,868</b>	<b>20,747</b>	<b>30,063</b>	<b>26,806</b>	<b>28,215</b>	<b>29,936</b>	<b>32,438</b>
<b>Borrowings</b>	<b>30,009</b>	<b>33,733</b>	<b>48,228</b>	<b>89,357</b>	<b>66,798</b>	<b>71,592</b>	<b>79,429</b>	<b>88,687</b>
Change (%)	16.6	12.4	43.0	85.3	-25.2	7.2	10.9	11.7
Other liabilities	1,506	2,287	2,963	3,581	2,771	3,325	3,990	4,788
<b>Total Liabilities</b>	<b>46,933</b>	<b>54,888</b>	<b>71,938</b>	<b>1,23,002</b>	<b>96,374</b>	<b>1,03,132</b>	<b>1,13,356</b>	<b>1,25,913</b>
Investments	0	1,870	10,070	3,009	2,306	2,306	2,306	2,306
Change (%)	-100.0	N.A	438.6	-70.1	-23.4	0.0	0.0	0.0
<b>Loans and Advances</b>	<b>42,779</b>	<b>51,549</b>	<b>59,004</b>	<b>1,03,637</b>	<b>78,019</b>	<b>83,246</b>	<b>93,446</b>	<b>1,04,337</b>
Change (%)	26.3	20.5	14.5	75.6	-24.7	6.7	12.3	11.7
Net Fixed Assets	38	88	597	3,664	4,176	4,384	4,603	4,834
Other Assets	4,117	1,381	2,266	12,692	11,874	13,196	13,000	14,436
<b>Total Assets</b>	<b>46,933</b>	<b>54,888</b>	<b>71,938</b>	<b>1,23,002</b>	<b>96,374</b>	<b>1,03,132</b>	<b>1,13,356</b>	<b>1,25,913</b>

E: MOFSL Estimates

## Financials and valuations

AUM Details						(INR m)		
Y/E March	2016	2017	2018	2019	2020	2021E	2022E	2023E
<b>AUM (INR b)</b>	<b>43</b>	<b>52</b>	<b>62</b>	<b>117</b>	<b>100</b>	<b>103</b>	<b>113</b>	<b>129</b>
<b>AUM Mix</b>								
<b>Corporate</b>	<b>94.8</b>	<b>87.6</b>	<b>73.7</b>	<b>38.6</b>	<b>28.8</b>	<b>27.1</b>	<b>24.7</b>	<b>23.3</b>
<b>Retail</b>	<b>5.2</b>	<b>12.4</b>	<b>26.3</b>	<b>61.4</b>	<b>71.2</b>	<b>72.9</b>	<b>75.3</b>	<b>76.7</b>
SME	5.2	12.4	23.4	16.1	17.5	16.4	14.6	13.2
Vehicle	0.0	0.0	2.1	40.7	45.3	46.0	48.2	49.5
Housing	0.0	0.0	0.8	4.7	8.3	10.5	12.5	13.9
<b>Ratios</b>						<b>(%)</b>		
Y/E March	2016	2017	2018	2019	2020	2021E	2022E	2023E
<b>Spreads Analysis (%)</b>								
Yield on Portfolio	13.9	13.4	13.6	13.1	15.1	15.3	15.0	15.0
Cost of Borrowings	10.4	9.8	7.9	8.2	10.2	10.2	9.8	9.6
Interest Spread	3.6	3.6	5.6	4.9	4.9	5.1	5.2	5.4
Net Interest Margin	7.2	7.0	7.9	6.4	6.6	6.9	7.0	7.3
<b>Profitability Ratios (%)</b>								
RoE	13.6	12.3	10.1	9.5	-11.4	4.4	5.9	8.0
RoA (on balance sheet)	4.4	4.1	3.2	2.5	-3.0	1.2	1.6	2.1
Debt: Equity (x)	1.9	1.8	2.3	3.0	2.5	2.5	2.7	2.7
Average Leverage (x)	3.1	3.0	3.2	3.8	3.9	3.6	3.7	3.8
<b>Efficiency Ratios (%)</b>								
Int. Expended/Int. Earned	51.3	48.5	42.7	52.1	56.8	55.9	54.4	52.9
Op. Exps./Net Income	16.4	17.8	33.4	38.4	47.8	46.7	45.2	43.7
Empl. Cost/Op. Exps.	67.8	66.3	68.8	60.6	53.6	64.2	64.9	65.0
Fee income/Net Income	22.4	18.5	5.6	19.4	18.0	16.4	17.1	17.0
<b>Asset quality</b>								
GNPA	100	727	768	3,051	3,652	6,042	6,499	7,068
NNPA	80	620	640	1,995	2,893	3,761	3,277	2,977
GNPA %	0.2	1.4	1.3	2.9	4.6	7.1	6.7	6.5
NNPA %	0.2	1.2	1.1	1.9	3.7	4.5	3.5	2.9
PCR %	20.0	14.8	16.7	34.6	20.8	37.8	49.6	57.9
<b>Valuation</b>								
Book Value (INR)	210.2	240.8	263.7	325.8	289.9	305.2	323.8	350.9
BV Growth (%)	11.7	14.6	9.5	23.6	-11.0	5.3	6.1	8.4
<b>Price-BV (x)</b>					<b>0.9</b>	<b>0.8</b>	<b>0.8</b>	<b>0.7</b>
EPS (INR)	26.1	26.9	25.5	26.1	-35.1	13.2	18.6	27.1
EPS Growth (%)	19.8	3.0	-5.3	2.5	-234.5	-137.6	41.1	45.4
<b>Price-Earnings (x)</b>					<b>-7.2</b>	<b>19.3</b>	<b>13.6</b>	<b>9.4</b>
Dividend per share					0.0	0.0	0.0	0.0
<b>Dividend Yield (%)</b>					<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
E: MOFSL Estimates								



Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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