BOBCAPS
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FIRST LIGHT

13 July 2022

RESEARCH

[Initiation] IIFL Wealth | Target: Rs 2,277 | +43% | BUY

Juggernaut rolling; initiate with BUY

BOB Economics Research | Monthly Chartbook

Depreciating INR: a major concern

BOB Economics Research | CPI and IIP

CPI sticky, IIP inched up

Daily macro indicators

Indicator	08-Jul	11-Jul	Chg (%)
US 10Y yield (%)	3.08	2.99	(9bps)
India 10Y yield (%)	7.42	7.43	1bps
USD/INR	79.25	79.44	(0.2)
Brent Crude (US$/bbl)	107	107.1	0.1
Dow	31,338	31,174	(0.5)
Hang Seng	21,726	21,124	(2.8)
Sensex	54,482	54,395	(0.2)
India FII (US$ mn)	**07-Jul**	**08-Jul**	**Chg ($ mn)**
FII-D	(2.8)	(1.3)	1.5
FII-E	(111.6)	15.0	126.6

Source: Bank of Baroda Economics Research

SUMMARY

[Initiation] IIFL Wealth

- Sustainable model with diverse product offerings in HNI/UHNI category and focus on expanding trail-based recurring revenue streams
- Expect strong fund flows to support 20% AUM CAGR and 18% earnings CAGR over FY22-FY25, aiding +6% ROAA and +28% ROAE
- Initiate with BUY given rising margins, strong clientele, favourable industry drivers and undervaluation; TP Rs 2,277 (25x FY24E P/E)

Click here for the full report.

India Economics: Monthly Chartbook

The most notable fact off late has been depreciating INR which is touching record low every other day. RBI came up with measures to support the external stability. Volatility in global yields has also been a concern, which has reversed the increase seen in Jun'22, on account of signs of recession visible in muted macro prints globally and inversion of the US yield curve. Globally, central banks have reaffirmed their commitment to maintain price stability with a majority of Fed Governors hinting at 75bps rate hike in Jul'22. On domestic front, RBI governor also spoke of 'increasing signs of sectoral price spillovers'. Today's inflation print will give further cues on the same.

Click here for the full report.

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India Economics: CPI and IIP

Headline CPI remained sticky at 7% in Jun'22 and ending Q1FY23 at 7.3% against RBI's estimate of 7.3%. IIP on the other hand rose sharply to 19.6% supported by favourable base. Sequentially as well industrial production improved and remained broad based reflecting capacity utilization of firms are picking up. On inflation front, some respite is seen on MoM basis as well as in seasonally adjusted data. But the big question is whether this momentum would sustain or not. The current print got comfort from government measures in terms of excise duty cut and edible oil prices. But still considerable upside risks to inflation cannot be ruled out considering services are still running at full capacity, pass through of prices by firms and price stickiness. Thus we maintain our estimate of 6.5% for headline CPI in FY23 and 4.4% for IIP. RBI is expected to continue with its rate action of another 50-75bps in the current cycle on account of catch up effect and price stability.

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BUY

TP: Rs 2,277 | ⮝ 43%

IIFL WEALTH | Diversified Financials | 12 July 2022

Juggernaut rolling; initiate with BUY

- **Sustainable model with diverse product offerings in HNI/UHNI category and focus on expanding trail-based recurring revenue streams**
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- **Initiate with BUY given rising margins, strong clientele, favourable industry drivers and undervaluation; TP Rs 2,277 (25x FY24E P/E)**

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Sustainable business model: IIFL Wealth's model of offering wealth solutions to high- and ultra-high-net-worth individuals (HNI/UHNI) is based on driving a larger share of recurring revenue streams (ARR), with its commission structures migrating to trail vs. upfront earlier. Thus, recurring revenue is independent of transaction volumes. At end-FY22, 55% of AUM and 65% of revenue was based on ARR, which we expect will grow to 61% and 81% respectively by FY25. The company managed 6,833 relevant families at end-FY22 (17% CAGR, FY17-FY22) with low attrition levels.

Expect 20% AUM CAGR and 18% earnings CAGR by FY25: The company's AUM grew 22% over FY17-FY22 to Rs 2.6tn (excluding custody assets). We expect net flows/net new money of Rs 340bn/Rs 405bn/Rs 452bn by end-FY23/FY24/FY25 with AUM reaching Rs 3.1tn/Rs 3.8tn/Rs 4.5tn. Similarly, we forecast a net profit CAGR of 18% over FY22-FY25 to Rs 9.6bn based on strong AUM growth coupled with operating leverage.

Decent AMC yields; on track to cross Rs 1tn in AUM by FY25: The AMC business (PMS, AIF and MFs, albeit AIF-heavy) continues to be one of IIFL Wealth's strongest segments, where AUM grew at a 44% CAGR over FY17-FY22 to Rs 556bn. We believe aggressive growth plans coupled with senior hires should take AUM past the Rs 1tn mark by FY25 (25% CAGR, FY22-FY25). The company expects to earn carry income in FY23/FY24, and we model for steady average yields of 79bps over FY23-FY25.

Margins on the rise: ROAE, which declined to 7% in FY20, grew to 20% at end-FY22 and ROAA, which declined to 1.8% in FY20, grew to 6%. We expect ~28% ROAE and ~7% ROAA by FY25 based on higher total income (14% CAGR over FY17-FY22) coupled with a projected decline in cost-to-income ratio to 44% in FY25 vs. 51% in FY22.

Initiate with BUY: IIFL Wealth is trading at 18x FY24E EPS and appears undervalued, in our view. We assign the stock a BUY rating with a TP of Rs 2,277 (43% upside) based on 25x FY24E EPS – a 10% premium to the 3Y average given a robust model, strong fundamentals and supportive macro factors.

Ticker/Price	IIFLWAM IN/Rs 1,596
Market cap	US$ 1.8bn
Free float	77%
3M ADV	US$ 1.0mn
52wk high/low	Rs 1,908/Rs 1,216
Promoter/FPI/DII	23%/22%/4%

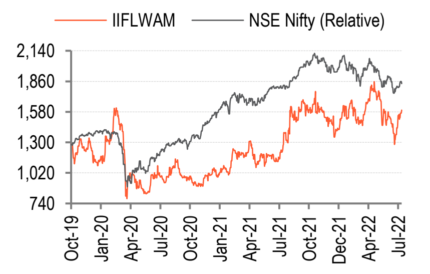
Source: NSE | Price as of 12 Jul 2022

Key financials

Y/E 31 Mar (Rs mn)	FY22P	FY23E	FY24E
PBT (Rs mn)	7,513	9,271	10,947
PBT growth (%)	54.9	23.4	18.1
Adj. net profit (Rs mn)	5,818	6,954	8,210
EPS (Rs)	64.1	77.1	91.1
Consensus EPS (Rs)	64.1	76.8	91.7
P/E (x)	24.9	20.7	17.5
MCap/AUM (%)	5.5	4.6	3.8
ROE (%)	20.0	22.7	25.5

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE

Depreciating INR: a major concern

The most notable fact off late has been depreciating INR which is touching record low every other day. RBI came up with measures to support the external stability. Volatility in global yields has also been a concern, which has reversed the increase seen in Jun'22, on account of signs of recession visible in muted macro prints globally and inversion of the US yield curve. Globally, central banks have reaffirmed their commitment to maintain price stability with a majority of Fed Governors hinting at 75bps rate hike in Jul'22. On domestic front, RBI governor also spoke of 'increasing signs of sectoral price spillovers'. Today's inflation print will give further cues on the same.

Mixed picture emerging: The economy continues to recover with some indicators signalling strength (air passenger traffic, services PMI print). However, it should be seen with caution as these are led by favourable base. Other consumption indicators such as auto sales, digital transactions and electricity demand have moderated on sequential basis. However, with steady decline in Covid-19 cases, google mobility indices are signalling an uptick. On the agri front, south-west monsoon is 7% above LPA (cumulative-8 Jul 2022). Kharif production has been lower (-9.3%) compared with last year. However, well-distribution of rainfall across country, will push kharif production higher.

Centre front-loading spending: Despite robust revenue growth, centre's fiscal deficit (% of GDP, 12MMA) in May'22 came in at 6.7%, up from 6.5% in Apr'22, as centre is on track to front load expenditure. So far (Apr-May'22), there has been 22.6% increase in overall spending (6.6% decline last year in the same period), led by 70% jump in capex (14% increase last year). Even revenue spending is up by 15.3%. Robust revenue growth has been able to provide key support to this plan. Centre's gross tax revenues in FYTD23 are up by 29%, led by 61% jump in direct tax collection and 9% increase in indirect tax collections. Recent data by the government also indicates that direct tax collections improved further in Jun'22. Net direct tax collections as of 16 June 2022 were recorded at Rs 3.4lakh crore (up by 45% YoY) compared with Rs 2.3lakh crore during the same period last year. Going forward, we do not expect any spending cuts and maintain our forecast for fiscal deficit at 6.6-6.7%.

Growth concerns impacted global yields: India's 10Y yield remained stable between Jun and Jul. However, global yields remained volatile. In Jun'22, while major yields rose, the situation completely reversed in Jul'22 with increased appetite for sovereign securities. This was on the back of aggravated concerns of recession following sombre PMI prints globally, inversion of US yield curve and falling commodity prices. This might provide domestic inflation some comfort along with the recent measures adopted by the government on domestic front. We expect India's CPI print to be at 6.8% in Jun'22 and at 6.5% in FY23. RBI is expected to hike rates by another 50-75bps.

INR to remain under pressure: INR depreciated to a fresh record-low of 79.36/$ in Jul'22 weighed down by a stronger dollar and persistent FPI outflows. Apart from this, domestic unfavourable domestic macros are also putting pressure on INR. Trade deficit touched a new record high of US$ 25.6bn in Jun'22, raising concerns on the external front. As a result, government announced measures such as hike in gold import duty to curb imports. RBI also announced a slew of measures to shore up foreign inflows. Even so an adverse global macroeconomic backdrop suggests that INR is likely to remain under pressure in the near-term.

Note: The source for all exhibits is 'CEIC and Bank of Baroda' unless otherwise specified

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CPI AND IIP

12 July 2022

CPI sticky, IIP inched up

Dipanwita Mazumdar
Economist

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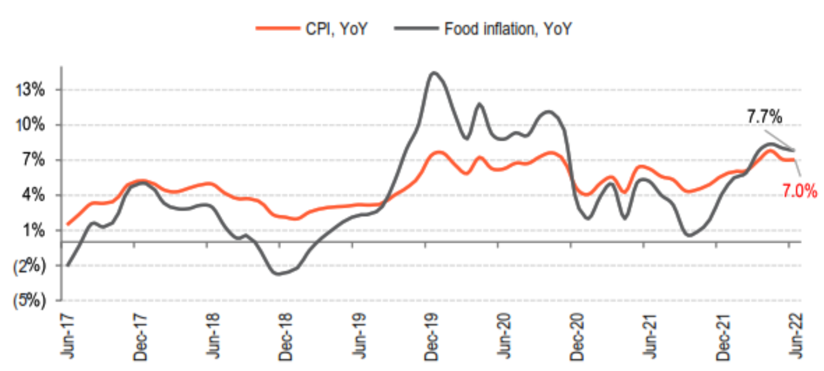
CPI inflation sticky at 7%: Against our estimate of 6.8% and compared to market consensus of 7.1%, headline CPI print for Jun'22 came in at 7% same seen in May'22, on YoY basis. For Q1FY23, the print stands at 7.3% against RBI's forecast of 7.5%. Food inflation moderated slightly to 7.7% from 8% in May'22. However, inflation rose for major components forming 55% of the overall food basket. These include: cereals whose inflation rose to 5.7% compared to 5.3%, meat and fish (8.6% from 8.2%), milk and products (6.1% from 5.6%), fruits (3.1% from 2.3%) and spices (11% from 9.9%). However, outlook for food inflation in the coming months might get some comfort from government measures to control edible oil prices, normal monsoon (till 7% above LPA) and some downside risks to demand from rising interest rate cycle.

Fig: 1 CPI still at 7%, food shows moderation



Source: CEIC, Bank of Baroda Research

Core inflation moderated slightly: Core inflation edged down by 10bps to 5.9% in Jun'22 from 6% in May'22, on YoY basis. The major drag down was on account of transport and communication inflation (6.9% from 9.5% in May'22), on account of cut in excise duty on petrol (Rs 8/lt) and diesel (Rs 6/lt).

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BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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