

Oct 25, 2023

RESULT REPORT Q2 FY24 | Sector: Credit Rating Agencies

ICRA Limited

Growth pick-up in H2 FY24 would be key

Performance below expectations

ICRA's Consolidated Rev. in Q2 FY24 was 5% below expectation and PBT was 13% below our estimate. The material miss on revenue came largely from Ratings segment, with Analytics segment revenue growth being moderate as expected. Consolidated EBITDA margin stood at 32.5% v/s estimate of 35.7%, leading to 14% EBITDA miss. The H1 FY24 margin at 33.1% stands 200 bps lower yoy. Slower growth in Ratings & Non-Ratings businesses, further increase in staff cost and structural investments in technology impacted margins. Ratings PBIT margin was 23% v/s 27% in Q1 FY24 and 25% in Q2 FY23, and it included 2% positive impact due to agreement on sharing of common expenses with ICRA Analytics. Ratings margin stands significantly lower than the long-term average. Higher tax rate in the quarter further dented earnings performance.

Ratings growth decelerated; recovery key in H2 FY24

Growth in Ratings Rev. (57% of consolidated revenues) significantly came-off to 8% yoy from averaging 16% yoy in preceding four quarters. During Q2 FY24, there was a dip in rated volumes in both Bond Rating and Bank Loan rating segments due to volatile yields and tight liquidity conditions. ICRA's market position/share was stable and there was no adverse pricing movement, as per the management. The co. continues to focus on better remunerative assignments and is endeavoring to push yields in sector/segments where it commands a strong rating preference. ICRA's thrust has been on the faster growing segments of Infrastructure, NBFCs-HFCs and Securitization. Basis its view that credit activity would remain firm, ICRA expects the momentum in Ratings business to continue.

Another quarter of moderated growth in Knowledge Services

ICRA Analytics saw modest growth (6%/5% yoy in Q2/Q1 v/s 20% yoy in FY23) in Knowledge Services (37% of consolidated revenues) on moderated business volumes from parent Moody's (contributes 80%+ of Rev.). Global slowdown/uncertainty impacted business flow/outsourcing of Moody's Corporation and there was slight increase in insourcing by the parent. Management expects addition of value-added segments and new areas of engagements with Moody's and developing of non-Moody's business both globally and in India to be future growth drivers.

Acquires D2K Technologies in Risk Analytics space

ICRA Analytics has acquired a majority stake in D2K Technologies Pvt Ltd (FY23 Rev. of ~Rs150mn), an established provider of software solutions to banks and other financial institutions in India offering tools/services that enable meeting of regulatory requirements while providing business intelligence and analytics. D2K specializes in Early Warning Systems and Income Recognition and Asset Classification identifiers, which complement ICRA's existing offerings. The acquisition is in-line with ICRA's growth and diversification strategy and would augment company's positioning in Risk Analytics/Solutions space. ICRA also plans to leverage D2K's capabilities for its own technology transformation journey.

Prune estimates/PT but retain BUY; re-rating hinged on revenue growth improvement

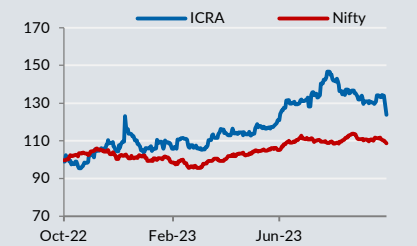
With performance below expectation in Q2 FY24 and transient choppiness likely continuing in Knowledge Services, we have trimmed earnings estimates by 2-3% for FY24/25 (downward revision could have been higher if not for upward revision in other income). We still assume an improvement (over Q2 FY24) in Ratings revenue growth and margins in coming quarters on conducive business conditions, positive pricing approach and operational improvements. We now expect 13%/14%/17% CAGR over FY23-25 in consolidated Rev./EBITDA/PAT. ICRA's overall growth and margin performance in H2 FY24 would be a key valuation catalyst for the stock. The company trades at 29x 1-year rolling fwd. P/E versus long-term average of 33x. Retain BUY with a lowered 12m PT of Rs6300 (earlier Rs6700).

Reco	: BUY
CMP	: Rs 5,187
Target Price	: Rs 6,300
Potential Return	: 21.5%

Stock data (as on Oct 23, 2023)

Nifty	19,282
52 Week h/l (Rs)	6249 / 3837
Market cap (Rs/USD mn)	53987 / 650
Outstanding Shares (mn)	10
6m Avg t/o (Rs mn):	32
Div. yield (%):	2.3
Bloomberg code:	ICRA IN
NSE code:	ICRA

Stock performance



	1M	3M	1Y
Absolute return	-6.2%	-5.6%	23.9%

Shareholding pattern

Promoter	51.9%
FII+DII	32.0%
Others	15.8%

Δ in stance

(1-Yr)	New	Old
Rating	BUY	BUY
Target Price	6,300	6,700

Δ in earnings estimates

	FY23	FY24e	FY25e
EPS (New)	141.7	166.5	193.8
EPS (Old)	141.7	167.8	196.3
% Change	-	-0.8%	-1.3%

Financial Summary

(Rs mn)	FY23	FY24E	FY25E
Net Revenue	4,032	4,471	5,139
Growth (%)	17.6%	10.9%	14.9%
EBITDA	1,429	1,556	1,859
Growth (%)	18.5%	8.9%	19.5%
PAT	1,367	1,607	1,870
ROE (%)	15.2%	16.0%	16.8%
EPS (Rs)	141.7	166.5	193.8
P/E (x)	36.6	31.2	26.8
BV (Rs)	985	1,093	1,219
P/BV (x)	5.3	4.7	4.3

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Exhibit 1: Result table

Rs. Mn	Q2 FY24	Q1 FY24	QoQ	Q2 FY23	YoY
Revenue	1,049	1,027	2.1%	986	6.3%
Total Expenses	708	681	4.0%	631	12.2%
EBITDA	341	346	-1.7%	355	-4.1%
EBITDA Margin	32.5%	33.7%	-123bps	36.0%	-352bps
Other Income	164	178	-7.8%	132	23.5%
Finance Cost	3	3	-3.2%	3	-11.1%
Depreciation	28	23	22.4%	24	17.4%
Profit before Tax	473	497	-5.0%	460	2.8%
Tax	151	91	65.9%	88	72.5%
Tax Rate	32.0%	18.3%	1367bps	19.1%	1292bps
Profit After Tax	321	406	-20.9%	372	-13.6%
As % of revenues	30.7%	39.6%	-890bps	37.7%	-708bps

Source: Company, YES Sec

Exhibit 2: Segmental Performance

Rs. Mn	Q2 FY24	Q1 FY24	QoQ	Q2 FY23	YoY
Ratings					
Revenue	600	597	0.5%	556	7.8%
PBIT	138	162	-15.0%	140	-1.6%
PBIT Margin	23.0%	27.2%		25.2%	
Consulting					
Revenue	12	15	-17.3%	14	-14.0%
PBIT	(15)	(10)	52.5%	(4)	254.0%
PBIT Margin	-120.7%	-65.5%		-29.3%	
Knowledge					
Revenue	391	375	4.3%	367	6.4%
PBIT	189	171	10.5%	200	-5.4%
PBIT Margin	48.3%	45.6%		54.4%	
Market					
Revenue	47	42	12.0%	49	-4.3%
PBIT	5	(1)	-	9	-47.1%
PBIT Margin	10.7%	-1.2%		19.3%	

Source: Company, YES Sec

KEY CON-CALL HIGHLIGHTS

Ratings Business

- Ratings growth is a leverage play on ratings market activity. In Q2 FY24, there was a dip in rated volumes in both bond rating and bank loan rating segments due to volatile yields and tight liquidity conditions.
- ICRA has not lost market share and its market position remains stable.
- Pricing approach/strategy remains unchanged. Continue to focus on more remunerative assignments and endeavoring to push yields up on the back of high rating preference/acceptability.
- ICRA's thrust has been on growth segments like Infra, NBFCs-HFCs and Securitization.
- ICRA has maintained credit growth/activity expectations for FY24 and expects momentum in Ratings Business to continue.
- Higher global yields could shift some borrowings of Large Corporates to domestic bond market.
- India's inclusion in Global Bond Index to spur growth and development of corporate bond market.

ESG Rating opportunity

- ICRA has applied to SEBI for license to carry out ESG Ratings.
- Co. would pursue ESG opportunity through both Ratings and Risk Analytics businesses.
- Revenue potential to evolve considerably over time. ESG Rating is not mandatory right now.

Knowledge Services

- Moderated growth in Knowledge Services underpinned by 1) global slowdown/uncertainty impacting business flow/outourcing of Moody's Corporation and 2) slight increase in insourcing by Moody's.
- Business flow from Moody's comprises of much steadier FTE-based outsourcing work (80-85%) and more volatile projects business (15-20%) which is dependent on outsourcing policy, global eco. and competition.
- Strong growth during FY21-23 in Knowledge Services was driven by demonstration of strong data extraction and analysis capability/delivery and addition of ESG support which has seen significant scale-up.
- Future growth levers would be addition of more value-added segments and new areas of engagements.
- ICRA is confident about capitalizing on new opportunities from Moody's – also looking at non-Moody's business both globally and in India.
- While headcount addition is a lead indicator of growth, there could be a reasonable lag between headcount build-out and revenue billing.

Risk Analytics / D2K acquisition

- ICRA Analytics has acquired a majority stake in D2K Technologies Pvt Ltd (FY23 Rev. of ~Rs150mn), an established provider of software solutions to banks and other financial institutions in India offering tools/services that enable meeting of regulatory requirements while providing business intelligence and analytics.
- ICRA also plans to leverage D2K's capabilities for its own technology transformation journey.

- D2K acquisition is in-line with group's growth and diversification strategy, helps in growing the risk analytics space, would add value to ICRA's current clients and expands addressable market to the entire BFSI space.
- D2K offerings are complimentary to existing ICRA offerings. D2K specializes in Early Warning Systems and Income Recognition and Asset Classification identifiers.
- D2K was profitable from the time it was set-up.
- ECL offerings for NBFCs of ICRA Analytics have been witnessing strong traction – impending migration to ECL provisioning for Banks would open a large opportunity.

Market Data

- Leading provider of fixed income valuation to AMC, Corporates and AIFs in India.
- Good traction witnessed for Rating Trackers and Credit Solutions.
- ICRA Analytics has tied-up with global data providers and now would be providing valuation data to Factset and Bloomberg.

Inorganic growth approach

- The group has been constantly looking out for inorganic opportunities in the non-ratings space.
- Key acquisition criteria are a) business should be a synergistic fit to current or planned areas of growth (Risk Analytics being foremost focus), b) business needs to be profitable or have a clear visibility of making profits, c) business should have established operations with good acceptability in market, and d) acquisition should value-add from Tech perspective.

Margins

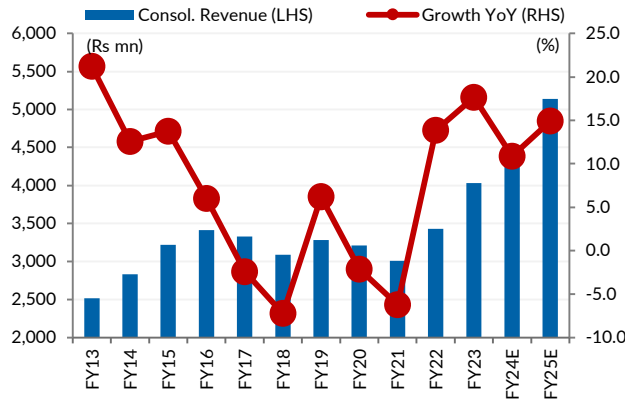
- Rating margins can improve aided by a) improved client acquisition/growth, b) pricing/realization improvement and c) operational efficiency/operating leverage.
- Salary cost and tech investments leading to be elevated opex. However, employee compensation benchmarking/corrections were completed in FY23.
- Tech investments include 1) some catch-up changes, 2) for enhancing products / client delivery, and 3) operational improvement through automation and 4) adoption of latest technologies like AI.
- Management expects overall margins to gradually improve over the medium term. Margin levers are likely to be operating leverage in ratings business, utilization improvement in Knowledge services, improvement in profitability of Market Data and Risk Analytics businesses and operational efficiencies derived from strategic tech investments.

Cash Utilization

- Group has been constantly evaluating capital allocation and thus concurrently evaluating acquisitions and dividend payouts.

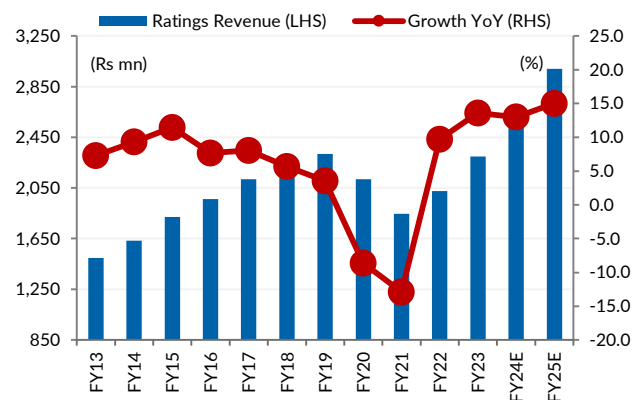
STORY IN CHARTS

Exhibit 3: Consolidated revenue growth to pick up



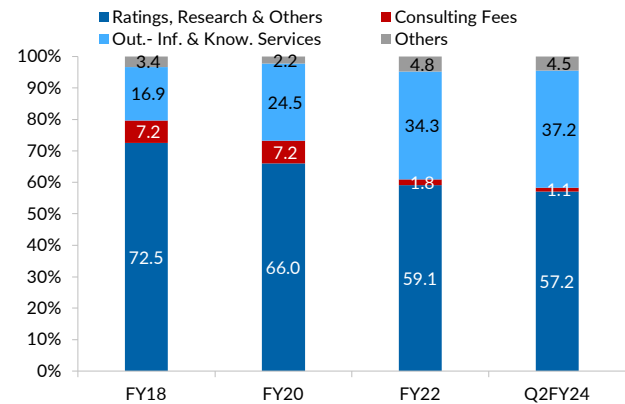
Source: Company, YES Sec

Exhibit 4: Expected revival in ratings revenue



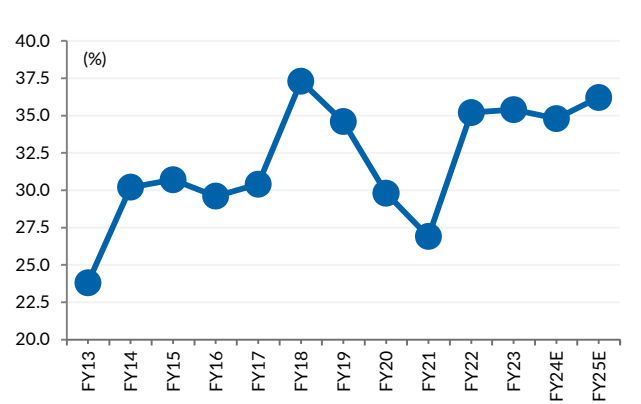
Source: Company, YES Sec

Exhibit 5: Revenue mix skewed in favor of ratings



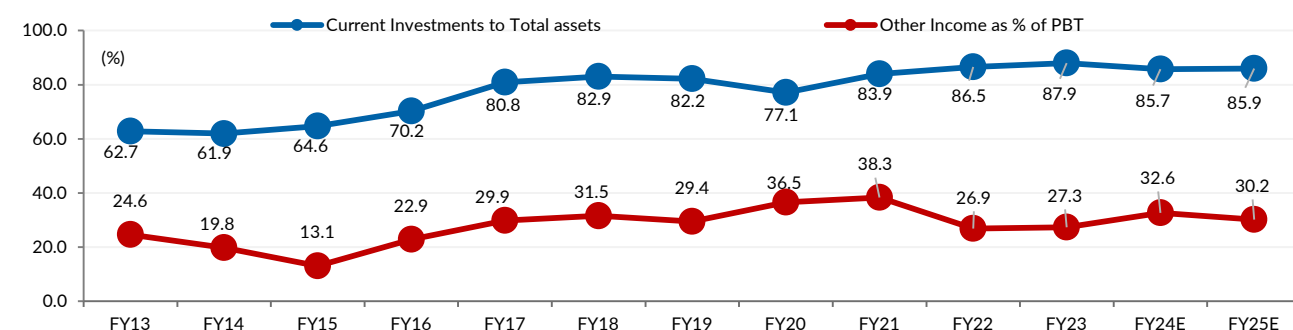
Source: Company, YES Sec

Exhibit 6: EBITDA margins enroute to recovery



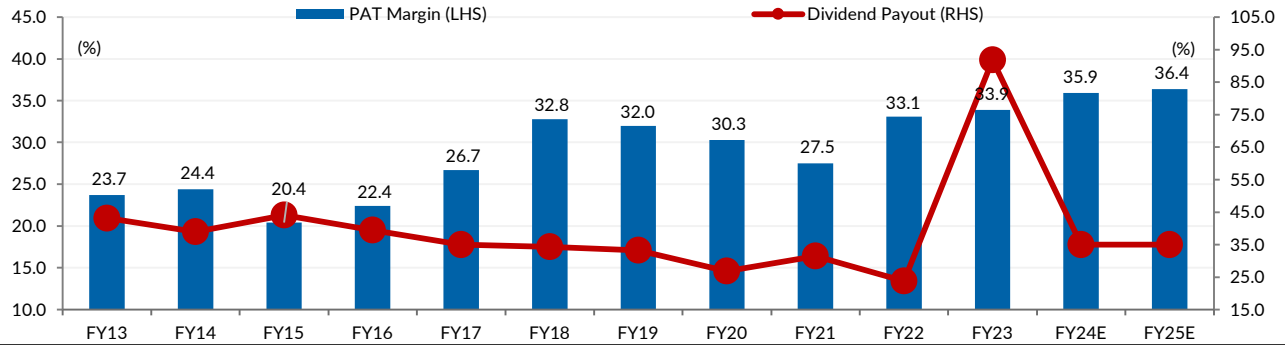
Source: Company, YES Sec

Exhibit 7: Consistent robust cash generation ensures significant liquidity on BS despite high DPR



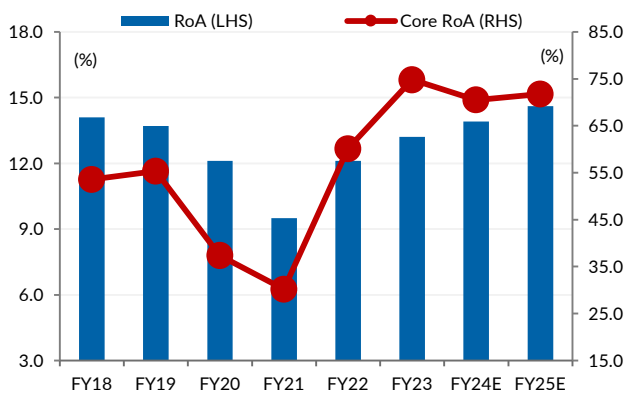
Source: Company, YES Sec

Exhibit 8: High profitability & dividend payout to continue

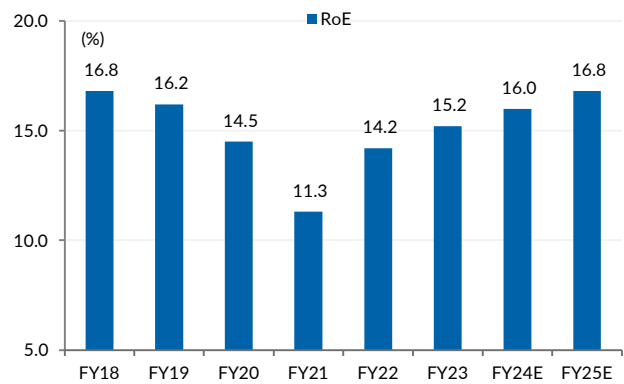


Source: Company, YES Sec

Exhibit 9: Core profitability metrics will improve underpinned by margin expansion and growth uptick

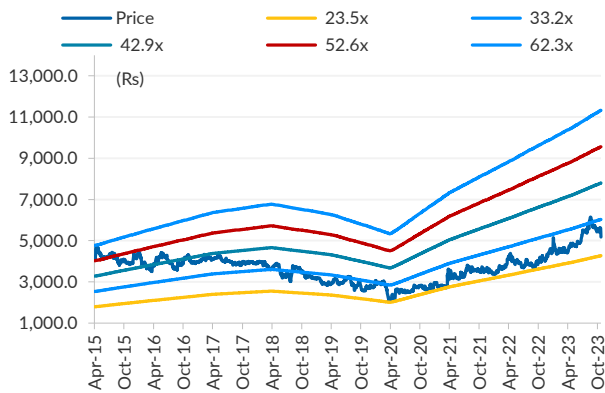


Source: Company, YES Sec



Source: Company, YES Sec

Exhibit 10: 1-yr rolling P/E band



Source: Company, YES Sec

Exhibit 11: 1-year rolling P/E vis-a-vis the mean



Source: Company, YES Sec

FINANCIALS

Exhibit 12: Balance Sheet

Y/e 31 Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Equity	97	97	97	97	97
Reserves	7,481	8,340	9,406	10,451	11,666
Net worth	7,577	8,436	9,503	10,547	11,763
Long-Term Provisions	34	31	27	29	30
Other financial liabilities	155	121	114	120	126
Total Non-Current Liabilities	189	153	141	149	156
Trade Payables	78	92	84	92	104
Other financial liabilities	120	81	88	80	72
Other Current Liabilities	662	609	721	807	908
Short-Term Provisions	293	365	423	431	440
Current tax liabilities (net)	9	7	2	2	2
Total Current Liabilities	1,161	1,155	1,317	1,412	1,525
Total Equity & Liabilities	8,960	9,785	11,008	12,154	13,490
Tangible Fixed Asset	269	254	275	325	375
Intangible Fixed Asset	183	190	184	184	184
Intangible Assets under development	32	16	13	13	13
Goodwill	12	12	12	12	12
Non-current investments	1,578	3,917	4,252	4,677	5,144
Deferred tax assets (net)	58	46	23	21	18
Long term loans and advances	1	1	0	0	0
Non-current tax assets	114	154	207	197	187
Other financial assets	1,754	825	373	410	451
Total Non-Current Assets	4,010	5,425	5,354	5,854	6,400
Investments	190	622	2,634	2,897	3,187
Trade receivables	475	265	380	735	845
Cash and cash equivalents	3,995	3,101	2,415	2,432	2,810
Other current assets	117	173	192	201	211
Other financial assets	172	199	33	35	37
Total Current Assets	4,950	4,359	5,654	6,300	7,090
Total Assets	8,960	9,785	11,008	12,154	13,490

Source: Company, YES Sec

Exhibit 13: Income statement

Y/e 31 Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Ratings, research & other service fees	1,846	2,025	2,300	2,599	2,989
Outsourcing	905	1,177	1,501	1,636	1,882
Consulting	88	62	57	63	51
Market	145	171	183	183	228
Others	26	-8	-9	-10	-11
Total Revenue	3,011	3,428	4,032	4,471	5,139
Employee Expenses	1,717	1,792	2,076	2,335	2,627
Other Expenses	482	430	528	580	653
EBITDA	811	1,206	1,429	1,556	1,859
Other Income	428	409	496	694	749
Depreciation	99	78	98	108	119
Interest Expense	21	16	14	12	10
PBT	1,120	1,521	1,812	2,129	2,479
Tax	293	386	445	523	609
PAT	827	1,135	1,367	1,607	1,870

Source: Company, YES Sec

Exhibit 14: Cash flow statement

Y/e 31 Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
PBT	1,120	1,521	1,812	2,129	2,479
Depreciation	99	78	98	108	119
Change in working cap	(1,180)	983	602	(289)	(30)
Tax paid	293	386	445	523	609
Cash flow from operations	(254)	2,197	2,067	1,426	1,959
Capex	(31)	(53)	(111)	(158)	(169)
Change in investments	(728)	(2,771)	(2,347)	(689)	(757)
Cash flow from investments	(759)	(2,823)	(2,458)	(847)	(926)
Free cash flow	(1,013)	(627)	(391)	579	1,033
Equity raised/(repaid)	(5)	(6)	954	(0)	-
Dividend (including tax)	261	270	1,255	562	655
Cash flow from financing	(266)	(276)	(301)	(562)	(655)
Net change in cash	(1,279)	(903)	(692)	17	378
Op Cash	5,268	3,995	3,101	2,415	2,432
CI Cash	3,995	3,101	2,415	2,432	2,810

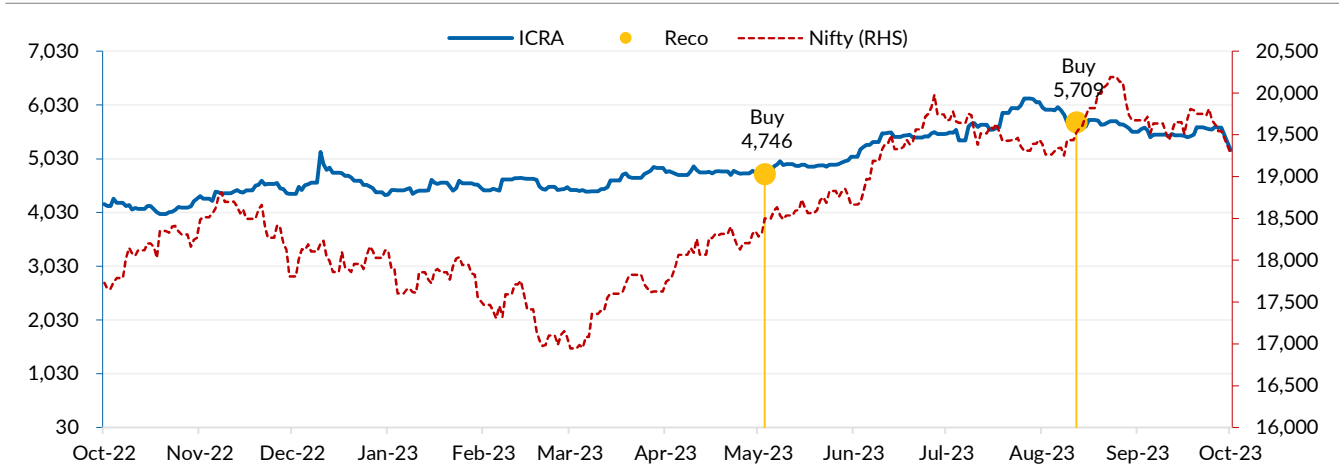
Source: Company, YES Sec

Exhibit 15: Growth and Ratio matrix

Y/e 31 Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Growth ratios (%)					
Ratings	-12.9%	9.7%	13.6%	13.0%	15.0%
Outsourcing	15.1%	30.1%	27.5%	9.0%	15.0%
Other revenues	-63.9%	-130.3%	12.9%	10.0%	10.0%
EBITDA	-15.3%	48.6%	18.5%	8.9%	19.5%
Net profit	-15.0%	37.3%	20.4%	17.5%	16.4%
Operating Ratios					
EBITDA Margin	26.9%	35.2%	35.4%	34.8%	36.2%
PAT Margin	27.5%	33.1%	33.9%	35.9%	36.4%
ROE	11.3%	14.2%	15.2%	16.0%	16.8%
Dividend Payout Ratio	31.5%	23.8%	91.8%	35.0%	35.0%
Per share					
EPS	86	118	142	166	194
Book Value	727	785	874	985	1,093
Valuation Ratios					
P/E	60.5	44.1	36.6	31.2	26.8
P/BV	6.6	5.9	5.3	4.7	4.3
Dividend Yield	0.5%	0.5%	2.5%	1.1%	1.3%

Source: Company, YES Sec

Recommendation Tracker



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5	YSL has received any compensation from the subject company in the past twelve months	No
6	YSL has received any compensation for investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
7	YSL has received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
8	YSL has received any compensation or other benefits from the subject company or third party in connection with the research report	No
9	YSL has managed or co-managed public offering of securities for the subject company in the past twelve months	No
10	Research Analyst or YSL has been engaged in market making activity for the subject company(ies)	No

Since YSL and its associates are engaged in various businesses in the financial services industry, they may have financial interest or may have received compensation for investment banking or merchant banking or brokerage services or for any other product or services of whatsoever nature from the subject company(ies) in the past twelve months or associates of YSL may have managed or co-managed public offering of securities in the past twelve months of the subject company(ies) whose securities are discussed herein.

Associates of YSL may have actual/beneficial ownership of 1% or more and/or other material conflict of interest in the securities discussed herein.

Analyst
Signature

Analyst
Signature

RECOMMENDATION PARAMETERS FOR FUNDAMENTAL REPORTS

Analysts assign ratings to the stocks according to the expected upside/downside relative to the current market price and the estimated target price. Depending on the expected returns, the recommendations are categorized as mentioned below. The performance horizon is 12 to 18 months unless specified and the target price is defined as the analysts' valuation for a stock. No benchmark is applicable to the ratings mentioned in this report.

BUY: Upside greater than 20% over 12 months

ADD: Upside between 10% to 20% over 12 months

NEUTRAL: Upside between 0% to 10% over 12 months

REDUCE: Downside between 0% to -10% over 12 months

SELL: Downside greater than -10% over 12 months

NOT RATED / UNDER REVIEW

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YES Securities (India) Limited ("YSL") is a wholly owned subsidiary of YES BANK LIMITED. YSL is a Securities and Exchange Board of India (SEBI) registered Stock broker holding membership of National Stock Exchange (NSE), Bombay Stock Exchange (BSE), Multi Commodity Exchange (MCX) & National Commodity & Derivatives Exchange (NCDEX). YSL is also a SEBI-registered Category I Merchant Banker, Investment Adviser and Research Analyst. YSL is also a Sponsor and Investment Manager of Alternate Investment Fund - Category III (YSL Alternates) and AMFI registered Mutual Fund Distributor. The Company is also a registered Depository Participant with CDSL and NSDL. YSL offers, inter alia, trading/investment in equity and other financial products along with various value added services. We hereby declare that there are no disciplinary actions taken against YSL by SEBI/Stock Exchanges.