

CARE RATINGS

RESULT UPDATE

KEY DATA

Rating	BUY
Sector relative	Outperformer
Price (INR)	631
12 month price target (INR)	825
Market cap (INR bn/USD bn)	19/0.3
Free float/Foreign ownership (%)	100.0/47.6
What's Changed	
Target Price	↑
Rating/Risk Rating	—

QUICK TAKE

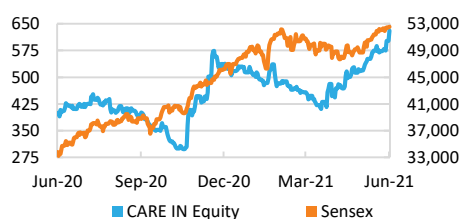
	Above	In line	Below
Profit	●		
Margins	●		
Revenue Growth	●		
Overall	●		

FINANCIALS

(INR mn)

Year to March	FY21A	FY22E	FY23E	FY24E
Revenue	2,484	2,702	2,989	3,344
EBITDA	958	1,046	1,168	1,354
Adjusted profit	895	948	1,041	1,203
Diluted EPS (INR)	30.4	32.2	35.3	40.8
EPS growth (%)	8.7	5.9	9.8	15.5
RoAE (%)	16.0	15.7	16.3	17.7
P/E (x)	20.8	19.6	17.8	15.4
EV/EBITDA (x)	14.3	13.0	11.3	9.4
Dividend yield (%)	2.7	3.0	3.1	3.5

PRICE PERFORMANCE



Explore:



Financial model



Podcast



Corporate access



Video

Structural transformation underway

CARE Ratings (CARE) beat estimates with 21% consolidated top-line growth in Q4FY21. It outperformed peers amidst marginally lower credit growth leading to 1% growth in overall FY21 sales. With 39% decline in other expenses, EBITDA grew 2x YoY (40% above estimates).

With the new management team in place, CARE is looking to regain market share and accelerate revenue growth, enhance technological prowess, HR and rebrand the group. CARE arrested market share loss in FY21. We expect its market share to grow led by sharpened focus, and revise multiple to 25x (22x earlier) Q1FY23E, 32% discount to peers. In the wake of improved performance, we revise up FY22/23E EPS 10/12%. Maintain 'BUY' with revised TP of INR825.

Robust performance

Q4FY21 ratings revenue jumped 19% YoY (31% ahead of estimate)--highest over the past three years--outperforming peers (CRISIL with domestic ratings growth of 6% YoY and ICRA's ratings revenue dip of 8% YoY). This was amidst a marginally lower credit growth of 3.4% (4% in Q4FY20) as industry credit growth picked up to 5.7% (4% in Q4FY20), while services slumped to 2% (from 9%). Long-term bond issuances slipped 13% YoY for the industry. With 39% YoY dip in other expenses, EBITDA rose 2x YoY. For FY21, revenue grew 2% YoY, with ratings up 1% YoY amidst a soft credit market (at 5.6%) and debt issuances supported with TLTROs. Going forward, management expects bond markets to be stable and wholesale credit to pick up.

Transformation underway

CARE is undergoing a transformational journey with changes across the entire C-Suite--new CFO, new Ratings Officer and cultural officer. Focus on overhauling the current processes is underway. Management will focus on four aspects: i) Ensuring one-third revenue from subsidiaries over 2-3 years. ii) Improve technology (tied up with US-based Tresata, leader in AI software) along with quality of ratings. iii) Enhance HR with focus on talent management. iv) Rebrand CARE group. This should aid in recouping market share lost post IL&FS crisis starting FY21.

Outlook and valuations: Gains anticipated; maintain 'BUY'

While the first two months of FY22 have been weak for debt markets, we anticipate CARE to recoup and gain market share under the new management team. We raise target multiple to 25x Q1FY23 and maintain 'BUY' with revised TP of INR825 (INR655 earlier), in line with five-years' average, 32% discount to CRISIL's target multiple.

Financials

Year to March	Q4FY21	Q4FY20	% Change	Q3FY21	% Change
Net Revenue	796	660	20.6	556	43.1
EBITDA	305	152	101.5	183	67.3
Adjusted Profit	261	153	70.6	186	39.9
Diluted EPS (INR)	8.8	5.2	70.6	6.3	39.9

Financial Statements

Income Statement (INR mn)

Year to March	FY21A	FY22E	FY23E	FY24E
Total operating income	2,484	2,702	2,989	3,344
COGS	0	0	0	0
Employee costs	1,199	1,280	1,388	1,505
Other expenses	328	376	433	485
EBITDA	958	1,046	1,168	1,354
Depreciation	78	79	81	82
Less: Interest expense	6	6	6	0
Add: Other income	313	326	330	356
Profit before tax	1,186	1,287	1,412	1,628
Prov for tax	277	324	356	410
Less: Other adj	0	0	0	0
Reported profit	895	948	1,041	1,203
Less: Excp.item (net)	0	0	0	0
Adjusted profit	895	948	1,041	1,203
Diluted shares o/s	29	29	29	29
Adjusted diluted EPS	30.4	32.2	35.3	40.8
DPS (INR)	17.0	19.0	19.6	22.0
Tax rate (%)	23.3	25.2	25.2	25.2

Important Ratios (%)

Year to March	FY21A	FY22E	FY23E	FY24E
Corp Debt (% of rev)	57.0	58.0	59.4	61.2
BLR (% of rev)	43.0	42.0	40.6	38.8
Gross margin (%)	51.8	52.6	53.6	55.0
EBITDA margin (%)	38.5	38.7	39.1	40.5
Net profit margin (%)	36.0	35.1	34.8	36.0
Revenue growth (% YoY)	2.0	8.7	10.6	11.9
EBITDA growth (% YoY)	17.8	9.2	11.6	15.9
Adj. profit growth (%)	8.7	5.9	9.8	15.5

Assumptions (%)

Year to March	FY21A	FY22E	FY23E	FY24E
GDP (YoY %)	(8.0)	9.0	7.0	7.0
Repo rate (%)	4.0	4.0	4.3	5.3
USD/INR (average)	75.0	73.0	72.0	71.0
CD Issuances (% YoY)	18.0	14.0	14.0	14.0
Bank Credit (% YoY)	16.0	16.0	16.0	16.0
Debt Rated Vol (INR mn)	9,112.0	9,840.9	11,120.2	12,788.3
BLR Assignments	3,399.0	3,806.9	4,187.6	4,606.3
SME Nos.	742.6	802.0	866.1	935.4
Other costs (% of sales)	13.2	13.9	14.5	14.5

Valuation Metrics

Year to March	FY21A	FY22E	FY23E	FY24E
Diluted P/E (x)	20.8	19.6	17.8	15.4
Price/BV (x)	3.2	3.0	2.8	2.7
EV/EBITDA (x)	14.3	13.0	11.3	9.4
Dividend yield (%)	2.7	3.0	3.1	3.5

Source: Company and Edelweiss estimates

Balance Sheet (INR mn)

Year to March	FY21A	FY22E	FY23E	FY24E
Share capital	295	295	295	295
Reserves	5,594	5,893	6,264	6,716
Shareholders funds	5,888	6,187	6,559	7,010
Minority interest	42	42	42	42
Borrowings	0	0	0	0
Trade payables	0	0	0	0
Other liabs & prov	666	681	695	710
Total liabilities	6,706	7,019	7,405	7,871
Net block	768	709	648	586
Intangible assets	83	83	83	83
Capital WIP	32	32	32	32
Total fixed assets	882	823	762	700
Non current inv	343	343	343	343
Cash/cash equivalent	4,876	4,966	5,360	5,823
Sundry debtors	214	496	549	614
Loans & advances	230	230	230	230
Other assets	160	160	160	160
Total assets	6,706	7,019	7,405	7,871

Free Cash Flow (INR mn)

Year to March	FY21A	FY22E	FY23E	FY24E
Reported profit	895	948	1,041	1,203
Add: Depreciation	78	79	81	82
Interest (net of tax)	4	4	4	0
Others	(245)	10	10	14
Less: Changes in WC	129	(282)	(53)	(65)
Operating cash flow	862	760	1,084	1,235
Less: Capex	(45)	(20)	(20)	(20)
Free cash flow	817	740	1,064	1,215

Key Ratios

Year to March	FY21A	FY22E	FY23E	FY24E
RoE (%)	16.0	15.7	16.3	17.7
RoCE (%)	21.1	21.3	22.1	23.8
Inventory days	nm	nm	nm	nm
Receivable days	46	48	64	63
Payable days	nm	nm	nm	nm
Working cap (% sales)	1.2	11.6	12.2	12.9
Gross debt/equity (x)	0	0	0	0
Net debt/equity (x)	(0.8)	(0.8)	(0.8)	(0.8)
Interest coverage (x)	142.5	156.6	176.1	0

Valuation Drivers

Year to March	FY21A	FY22E	FY23E	FY24E
EPS growth (%)	8.7	5.9	9.8	15.5
RoE (%)	16.0	15.7	16.3	17.7
EBITDA growth (%)	17.8	9.2	11.6	15.9
Payout ratio (%)	55.9	59.0	55.5	53.9

Q4FY21 Conference call: Key highlights

Financials

- In Q4FY21, CARE's consolidated top line grew 21% YoY, 31% above our estimate. Over FY21, revenues grew 2% YoY. Ratings revenue in Q4FY21 grew 19% YoY. Ratings revenue for FY21 grew 1% YoY led by soft bank credit (5.6% versus 6.1% in FY20) and lower CP issuances (down 21%), though long-term bond issuances were up 12% for the industry led by the RBI's TLTRO operations.
- **Industry:** For the industry, long-term bond issuances grew 12% YoY during FY21. Majority of this debt was raised by the financial sector (68%), out of which banks/term lending was 37%, financial services/investment was 17% and housing finance was 14%. Roads and highways, power generation and supply, oil exploration and refining, real estate and telecom comprised ~7%, 5%, 3%, 3% and 3% of total corporate bond issuances, respectively.
- **CP and wholesale credit down in FY21:** CP issuances were down 21% in FY21 to INR17.41tn. Furthermore, bank credit growth was up 5.6% (versus 6.1% in FY20). This is led by industry credit at 0.4% YoY and services credit at 1.4% YoY.
- EBITDA beats estimates: EBITDA grew 2x YoY to INR305mn (40% above estimates). This is on account of a sharp reduction in other expenses (at 39% YoY).
- PAT grew 71% YoY in Q4FY21, owing to a 70% YoY increase in taxes and 24% lower other income.
- Net cash position as of end-FY21 was INR4.9bn.

Operations and macroeconomic outlook

- For Q4FY21, all the four subsidiaries of CARE were PAT positive while 3 of the four subsidiaries were PAT positive for FY21.
- CARE appointed Mr. Jinesh Shah as CFO (erstwhile Head – Finance, and Accounts at India Ratings and Research), and Ms. Nehal Shah as the Company Secretary.
- Earlier it appointed Sachin Gupta as Chief Ratings Officer in March 2021 (earlier at CRISIL where he was a Senior Director and managed the Corporate and Infra Ratings.)
- CARE is strong in BFSI and infrastructure lending with 50-60% of ratings business depending on these industries.
- With the new management team in place, the team's focus is four-fold: 1) accentuating the group concept with ratings being the mainstay and accelerating growth from CART and CRSPL. 2) Increase use of technology to cut costs and enhance offerings, ease workflow systems and increase data focus. 3) Enhance HR as people remain the key resource, with emphasis on training. And 4) Rebrand CARE name to ensure it is associated with quality.
- Management is working on building share in the capital markets business as well, and it remains a key focus area with emphasis on profitable products like securitisation, along with REITs, InvITs, etc. Management remains focused on increasing market share in the ratings business.

- The focus for FY21 was on building core business applications on the new technology framework, which would integrate various applications within the organization and data sourcing tools from the market. This initiative will automate various manual processes with the help of AI / ML based models.
- CARE Ratings has signed a Memorandum of Understanding with US based Tresata Inc., a global leader in AI & predictive analytics software, on the 8th of August, 2020 to join forces to launch predictive intelligence business solutions in India. Tresata's Analytics Operating System will power their core ratings applications which will help to revolutionize intelligence about businesses in India. In turn, this will assist in making data driven decisions - data collected and validated both from issuers and also from a variety of broader market sources over the years. With this System, the rating analysts will leverage the latest artificial intelligence & machine learning techniques to analyze client data when evaluating risk – both current and emerging.
- There is a new CEO in place at CART (advisory business) – Mr Sudip Sural, an infrastructure and credit risk specialist with more than 25 years of experience in credit ratings, infrastructure finance and corporate financial risk assessment. Management has identified 2-3 revenue streams.
- CRSPL (Risk Solutions business) has seen significant opportunity to be scaled up with products for BFSI sector and CFOs and technological expertise is being built with focus on new products.
- EBITDA from the new business is likely to be lower than mainstay ratings business. However, management expects to scale up EBITDA margins of CRSPL to 30-35% over 5 years.
- Improving quality of ratings is of paramount importance and management has ensured the ratings process is independent and integrity of the process is retained.
- Earlier, CARE was paying its people, especially at the junior level below market rates and there was not a CEO for a large part of FY20. As a result, employee expenses in FY21 rose 10% YoY. While management will look to be leaner, employee remuneration should continue at a similar trajectory.
- FY22 is likely to be better than FY21, however, slightly slower than earlier anticipated, as CARE estimates GDP growth 8.8-8.9% from 11-11.2%.
- The modified credit ratio (MCR) at the end of Q4FY21 remained at 0.99, and remained moderate in FY21. There has been a sequential improvement in the ratio over H2FY21. The MCR is the credit quality of rated entities, as measured by CARE Ratings.
- CARE Ratings has taken the lead to incorporate an "Association of Indian Rating Agencies" to build confidence across all stakeholders.
- Formulation of Association of Indian Rating Agencies is awaiting some board approvals for some of the companies before they can join and should build communication channels with the regulators and remains a work-in-progress at present.

CARE RATINGS

Exhibit 1: Quarterly financial snapshot (consolidated)

Year to March	Q4FY21	Q4FY20	YoY	Q3FY21	QoQ	FY21	FY22E	FY23E
Revenues	796	660	20.6	556	43.1	2,484	2,702	2,989
Employee cost	349	277	26.0	301	15.9	1,199	1,280	1,388
Other expenses	142	231	(38.8)	73	95.1	328	376	433
Total expenditure	490	508	(3.5)	373	31.3	1,527	1,656	1,821
EBITDA	305	152	101.5	183	67.3	958	1,046	1,168
Depreciation	17	20	(13.9)	20	(14.8)	78	79	81
EBIT	288	131	119.2	162	77.6	880	967	1,087
Interest	0	2		2		6	6	6
Other income	57	74	(23.8)	81	(30.2)	313	326	330
Add: Exceptional items	0	0		0				
Profit Before Tax	344	204	69.1	242	42.5	1,186	1,287	1,412
Less: Provision for Tax	80	47	69.8	52	51.9	277	324	356
Less: Minority Interest	4	4		3				
Reported Profit	261	153	70.6	186	39.9	895	948	1,041
Adjusted Profit	261	153	70.6	186	39.9	895	948	1,041
No. of Dil. shares outstanding (mn)	29	29		29		29	29	29
Adjusted Diluted EPS	8.7	5.1	72.3	6.2	40.0	30.4	32.2	35.3
as % of net revenues								
Staff expenses	43.8	42.0		54.1		48.2	47.4	46.4
Other expenses	17.8	35.1		13.1		13.2	13.9	14.5
EBITDA	38.4	23.0		32.8		38.5	38.7	39.1
Net profit	32.8	23.2		33.5		36.0	35.1	34.8

Source: Company, Edelweiss Research

Exhibit 2: We upgrade our FY22/23E EPS by 10/12%

(INR mn)	Old		New		% change	
	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
Revenue	2,549	2,841	2,702	2,989	6.0	5.2
EBITDA	915	1,001	1,046	1,168	14.3	16.7
PAT	861	928	948	1,041	10.1	12.2

Source: Edelweiss Research

Company Description

Credit Analysis & Research Ltd (CARE) is primarily engaged in rating services which accounts for around 98% of the total revenue of the company. CARE is the second largest rating company in India in terms of rating turnover. As on FY20, company has rated INR7.2trillion of debt.

In the last few years, the company has begun expanding internationally and is providing technical assistance services to countries like Maldives, Hongkong, Nepal and Mauritius. In addition, CARE entered into collaboration with four credit rating agencies from emerging markets like in Brazil, Portugal, Malaysia, and South Africa each to provide ratings in those countries, set up ARC ratings in those countries. CARE also provides research services and it has been expanding its product portfolio to include newer services. The company is exploring opportunities to provide risk management solutions and acquired 75.1% stake in Kalypto, a firm providing risk management software solutions in Nigeria in Nov 2011.

Investment Theme

With majority of revenues (98%) coming from ratings as compared to diversified profile of other companies, the company is well placed to leverage the cyclical and structural uptick in the bank loan and corporate debt ratings. Management is focusing on: i) automation across businesses and improving ratings models; ii) focus on margin-accretive accounts within capital markets; iii) improving the contributions of subsidiaries; and iv) overhauling internal processes towards stringent compliance regulations. We anticipate an improvement in CARE's market share. We have built in 10.4% EBIDTA CAGR over FY21-23E.

Key Risks

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. They have further provided for the penalty laid by SEBI related to IL&FS default.

Concentration risk

CARE's business is concentrated on rating revenues, which account for 98% of consolidated revenues as compared to CRISIL and ICRA which are more diversified in revenue profile. As a result macroeconomic concern would impact the growth of the company. However, the company has taken small steps towards diversification with the acquisition of Kalypto, a risk management company in Nigeria. Also the company is developing its business outside India having entered Maldives, Nepal, Mauritius, Brazil, Portugal, Malaysia and South Africa through various route like technical assistance to local agencies and JV route.

High margin sustenance

CARE has one of the highest operating margins in the industry due to its cost competitiveness and technology-driven ratings methodology. The company's foray into newer geographies and services may potentially impact margins in the medium term. The margins have started now normalising in line with the industry, as they have been investing in more experienced employees.

Additional Data

Management

Chairman	Najib Shah
MD & CEO	Ajay Mahajan
CFO	Jinesh Shah
Chief Ratings Officer	Sachin Gupta
Auditor	Khimji Kunverji & Co

Holdings – Top 10*

% Holding		% Holding	
Bajaj Allianz Life	3.88	ABSL AMC	1.87
Polar Capital	3.88	Russel Investments	1.80
Franklin Resources	3.58	PineBridge Investments	1.80
First Pacific Advisor	3.45	Bajaj Holdings	1.42
Vanguard Group	2.43	Alternate Investments	1.22

*Latest public data

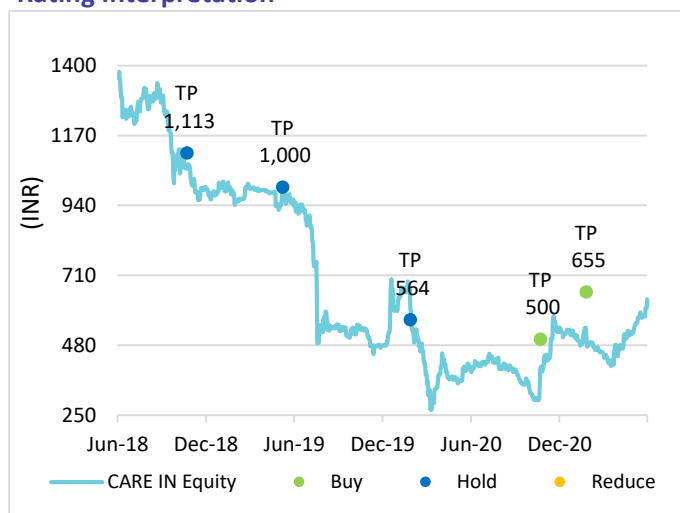
Recent Company Research

Date	Title	Price	Reco
11-Feb-21	Transformation underway; <i>Company Update</i>	509	Buy
08-Feb-21	Growth on the anvil; <i>Result Update</i>	509	Buy
05-Nov-20	The tide turns ; <i>Result Update</i>	404	Buy

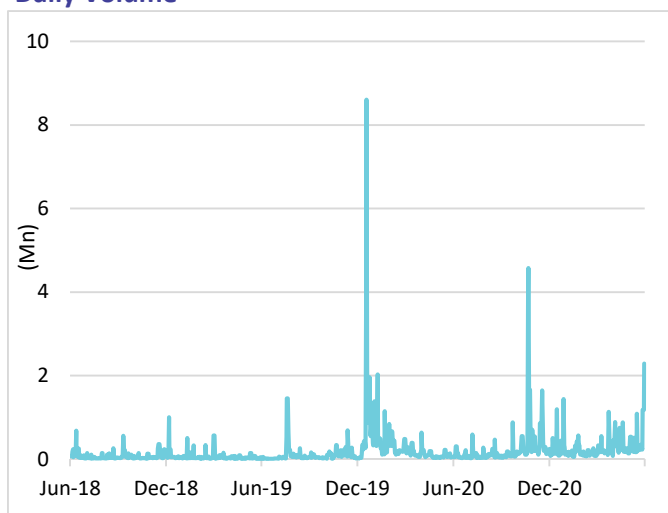
Recent Sector Research

Date	Name of Co./Sector	Title
23-Apr-21	CRISIL	Global recovering, domestic tempering; <i>Result Update</i>
15-Feb-21	CRISIL	Improved traction across the board; <i>Result Update</i>
24-Oct-20	CRISIL	Ratings decline, research strong; <i>Result Update</i>

Rating Interpretation



Daily Volume



Rating Distribution: Edelweiss Research Coverage

	Buy	Hold	Reduce	Total
Rating Distribution*	164	61	17	243
	>50bn	>10bn and <50bn	<10bn	Total
Market Cap (INR)	209	44	3	256

*1 stocks under review

Rating Rationale

Rating	Expected absolute returns over 12 months
Buy:	>15%
Hold:	>15% and <-5%
Reduce:	<-5%

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