

April 1, 2008

Not rated

Price	Target Price
Rs689	NA

Sensex	15,644
---------------	---------------

Price Performance

(%)	1M	3M	6M	12M
Absolute	(9)	(32)	(33)	n.a
Rel. to Sensex	3	(12)	(26)	n.a

Source: Bloomberg

Stock Details

Sector	Banks
Reuters	ICRA.BO
Bloomberg	ICRA @IN
Equity Capital (Rs mn)	100
Face Value	10
52 Week H/L	1158/525
Market Cap	Rs6.9bn/US\$172mn
Daily Avg Volume (No of shares)	14,390
Daily Avg Turnover (US\$)	0.3mn

Shareholding Pattern (%)

(31st Dec.'07)

Promoters	28.5
FII	0.5
Institutions	46.5
Private Corp.	6.9
Public	17.71

Source: Capitaline

Kashyap Jhaverikashyap.jhaveri@emkayshare.com

+91 22 6612 1249

Pradeep Agrawalpradeep.agrawal@emkayshare.com

+91 22 6612 1340

ICRA Ltd.**In sweet spot**Management
meet update

The credit rating business in India is in a sweet spot as it is on the cusp of robust growth potential driven by three triggers a) strong CapEx cycle in Indian economy b) lower penetration of corporate bond market and c) regulatory push due to implementation of Basel II norms. ICRA, one of the four leading rating agencies in India, is likely to benefit from this favorable scenario with its strong parentage (Moody) and its domain expertise.

ICRA has over past three years used its strong cash flows and domain expertise to expand its services offering beyond main bread and butter rating business. The IT and outsourcing services have given further boost to revenues. The boost to profitability will be more meaningful as once it achieves commendable scale in these new businesses.

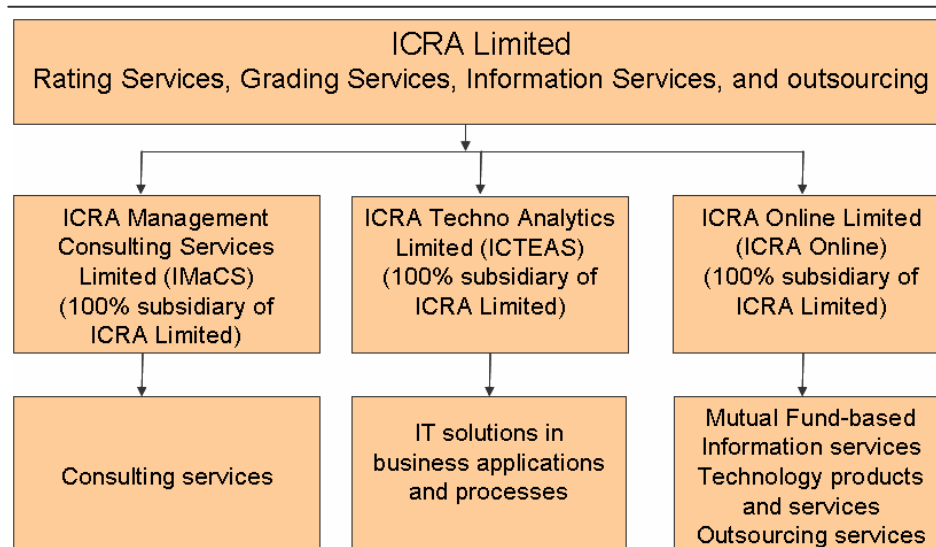
The stock is currently quoting at 25.3x FY08E EPS and 3.9x FY08E book value with core RoE of 19.6%. A chest of ~Rs1bn of cash plus investments (16% of MCap), provides opportunities for brownfield expansion as well.

Company background

ICRA is one of the four credit rating agencies in India providing a wide range of products and services. It was established in 1991 by IFCI and other financial institutions, commercial banks and financial services companies. Moody's (an international rating agency) is a strategic partner in the company having 28.5% stake. Moody's provides ICRA with technical services and also outsources certain services to ICRA.

Business operations

Credit rating services is key business for the company. It also has wholly-owned subsidiaries, namely, ICRA Management Consultancy Services (IMaCS), ICRA Techno Analytics (ICTEAS) and ICRA online that provide management consulting services, business solutions and computer aided engineering services and information services and outsourcing services respectively. ICRA Online, to complement its information services business, also provides technology solutions targeted at distributors of third party financial products, insurance brokers and stock broking houses.

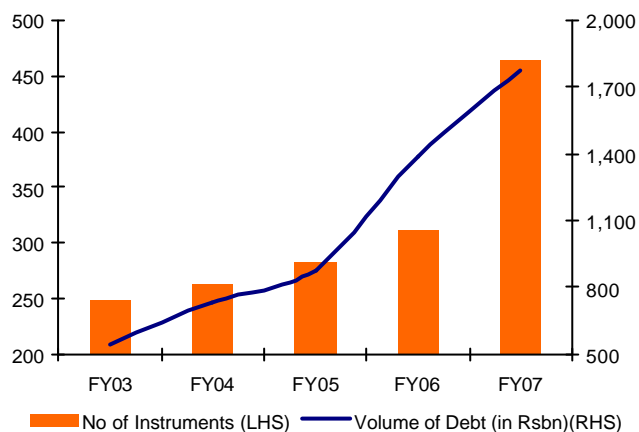
Business flow chart

Source: Company, Emkay Research

Rating business = volumes + penetration + regulation

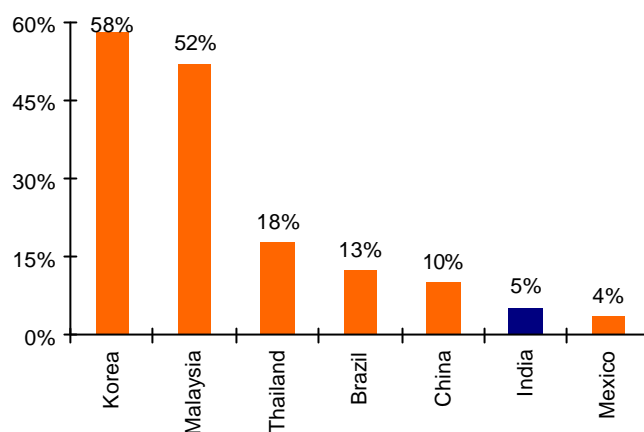
Rating business contributes ~50% of the operating revenues of ICRA. The acceleration in the economic activities in India, particularly the fixed asset investment activities (CAGR of 24% over FY04-07) coupled with lower penetration level of the corporate bond (5%) has resulted in a CAGR of 34% in the rating business volumes for ICRA over FY03-07.

Rating business – volumes for ICRA



Source: Company DRHP

Penetration of corporate bonds as % of total borrowings



Source: Company DRHP

While, the abovementioned triggers continue to be robust (investment activity still continuing and penetration remaining low), the rating business is likely to get regulatory push with the implementation of Basel II norms.

The Basel II norms require lower risk weightages for the higher credit rated corporates. We believe that the credit rating will find increased acceptance amongst the banks as well as borrowers for two simple reasons. For borrower a higher credit rating would mean lower credit cost. For bank it means effective use of capital as higher credit rating means lower risk weight and hence less capital requirement. ICRA has already signed MOU (non-exclusive) with 13 banks to assign ratings to the Bank's loans and other exposures under the standardized approach of RBI's New Capital Adequacy Framework for Basel-II.

Key segments	Share in rating revenues	Growth Drivers
Corporate & Infrastructure	34%	Growth in economy – investments in capacity Basel II norms – banks want efficient use of capital Regulatory changes – compulsory grading of IPOs (17 till date for ICRA)
Financial Sector	51%	Credit growth – banks looking at raising tier II and quasi tier I capital Growing presence of NBFCs – Originate to securitize model
Structured finance	13%	Basel II norms – lower risk weight on enhancements if the instrument is rated (Currently 100% deduction from tier I capital) Regulatory changes – SCRA amendment to include PTCs to allow them to be listed on stock exchanges
Public finance	2%	To be stable business, fresh issuance by the government not rising

Source: Company, Emkay Research

Advisory services = domain expertise + corporate relationships

The advisory business contributes 20% of ICRA's operating revenues. The advisory business has been natural extension of ICRA's rating business as it has gotten requisite domain knowledge as well as corporate relationships. ICRA provides advisory services to private as well as public sector companies with focus on sectors like infrastructure, energy, banking and insurance in legal as well as functional areas.

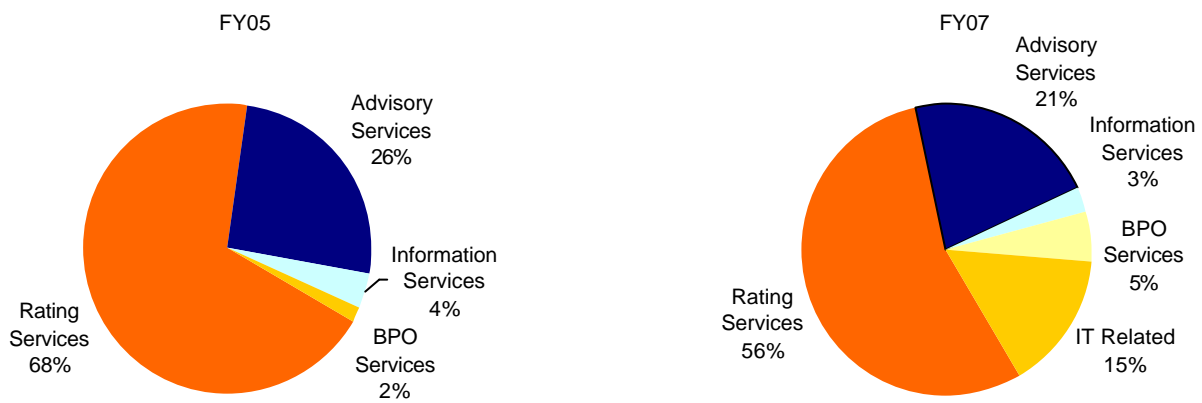
Over next five years, India is likely to see a massive USD500bn investment in infrastructure and energy space and ICRA being key player in this segment, is likely to be key beneficiary.

Surplus liquidity used to diversify businesses

ICRA made couple of acquisitions in the recent past to diversify its presence in other areas. In FY06, the Company acquired 100% stake in Computer Exchange Private Limited (name changed to ICRA Techno Analytics Limited) and ICRA Online Ltd, which diversified the company's presence into information technology solutions and knowledge process outsourcing services.

The company has around Rs633mn worth of surplus cash, invested in liquid mutual funds. As the rating business doesn't require much capital expenditure, the company could use this surplus cash for further acquisitions in non rating segments such as BPO services, information services and IT related services, to further strengthen its presence in these areas.

Revenue mix

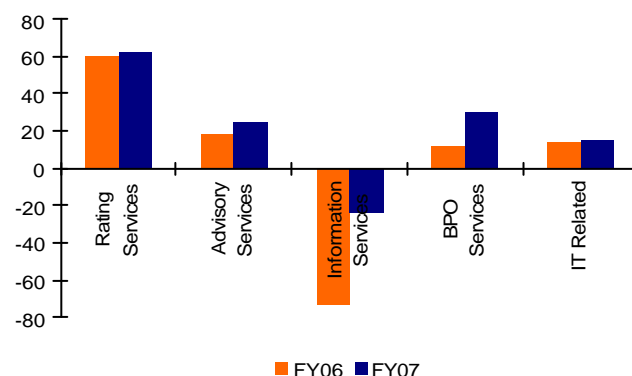


Source: Company

Scale up leading to improved Margins

Being an established player in rating industry, ICRA is raising its presence in other business segments like consultancy, information technology service and outsourcing activities. As the ratings business is linked to the capital market, any slowdown in the latter would directly impact earnings. So the company is broadening its product range and moving into other segments. As the company is expanding its scale of operations, it is benefiting from economies of scale, thereby resulting in improved margins. The company's non-ratings business contribution to the total earnings has increased from 30% in FY04 to 49% in FY07. The EBITDA margin has improved across business segments. The company's overall margin has improved by 300bps, with 30% rise in total sales.

Operating Margin (%)



Source: Company, Emkay Research

Strong relationship with Moody

The company has a close association with its promoter, the Moody's Group. The company has technical services agreement with Moody pursuant to which it receives certain high-value technical services. Moody's also advises ICRA on Rating-products strategy and the Ratings business in general.

Moreover, the Company and its subsidiaries provide certain outsourcing services to the Moody's Group. The company has entered into service agreement in FY05, with Moody's Investors Service to provide information management services to it. We believe that the growing relationship between the two will provide the company with larger business opportunities, going forward.

Financial performance for M9FY08

The company's total revenue grew 41.2%yoy to Rs429mn in M9FY08. The growth was primarily driven by higher rating and consulting revenues, which registered a growth of 50.6% and 39.5% respectively during the period. The EBITDA margin expanded by 228bps as the expenditure (as percentage of revenue) declined during the period driven by lower administrative expenses. Despite higher operating income the net income grew by only 42.3% to Rs193mn, as it was partially offset by higher taxes, which grew 65.3%yoy in the period.

Rs mn	M9FY08	M9FY07	% yoy chg	Q3FY08	Q3FY07	Q2FY08	% yoy chg	% qoq chg
Operating income								
<i>Rating Services</i>	429	285	50.6	149	89	159	67.3	-6.4
<i>Consulting</i>	122	88	39.5	45	39	49	14.7	-7.6
<i>Information Services</i>	19	15	28.0	6	8	7	-24.8	-24.3
<i>KPO/BPO Services</i>	45	30	48.0	17	18	14	-3.8	17.3
<i>Professional Services</i>	91	78	16.9	30	21	30	44.3	-2.2
Total	706	495	42.5	246	174	260	41.5	-5.4
Other Income	54	43	25.8	17	26	22	-35.2	-24.2
Total Income	759	538	41.2	263	200	282	31.7	-6.8
Total Expenditure	459	333	37.6	155	109	162	42.7	-4.5
EBITDA	247	162	52.4	91	65	98	39.4	-6.8
Depreciation	27	20	33.3	10	8	9	28.2	8.7
EBIT	273	184	48.4	98	83	111	17.5	-11.5
PBT	273	184	48.4	98	83	111	17.5	-11.5
Tax	80	48	65.3	30	15	29	94.8	3.4
PAT	193	136	42.3	68	68	82	-	-16.8

Source: Company, Emkay Research

Key risks and concern

- ICRA is primarily engaged in the business of rating services, 51% of its income come through the ratings business, which is linked to the issuance of debt securities in the capital market. Unfavourable economic conditions would directly affect the securities market and thereby earnings.
- ICRA being in the services sector, its performance is highly dependent on its ability to nurture and retain its employees. The company has been experiencing high attrition rate of around 22-23%, which is higher, though in line with its other peers in the industry. To counter this the company has adopted an Employee Stock Option (ESOP) Scheme, under which the company will grant options up to a maximum of 906,000 Equity Shares, constituting 9.06% of its paid-up equity capital. This is likely to control the high attrition rate and hence improve company's performance, going forward.
- Further strengthening of Rupees against US Dollar could negatively impact company's outsourcing business
- ICRA receives certain portion of its revenues from outsourcing services provided to Moody's. The turmoil in the global financial markets and the structured

products market has affected volumes of services being outsourced by Moody's. The performance of outsourcing business has been also affected by Rupee appreciation.

Valuations

ICRA and CRISIL are the only listed rating agencies in India. At the current market price of Rs569, the stock is quoting at 25.3x its FY08E EPS and 3.9x FY08E ABV with ROE of 19.6% compared to industry leader CRISIL which is trading at 26.0x its CY07 EPS and 8.1x CY07E ABV. Considering the growth potential in the ratings business and ICRA's presence in high growth consulting and outsourcing services, we believe the company is well placed for future growth.

Comparative valuations

	ICRA (FY08E)	CRISIL (CY07)
Revenue break up (Rs mn)		
Rating	526	1,301
Consulting	180	1,067
Others	293	185
Revenue CAGR (FY05/ CY04-FY08E/CY07) (%)	35.7	46.5
Net profit CAGR (FY05/ CY04-FY08E/CY07) (%)	49.8	44.3
CMP (Rs)	689	3058
EPS (Rs)	27.2	117.8
PER (x)	25.3	26.0
BV (Rs)	174.6	377.3
P/BV (x)	3.9	8.1
Core RoE (%)	19.6	33.0
Cash per share	91	109

Source: Capitaline, Emkay Research

Income Statement (Rs. Mn)

(Year Ending Mar 31)	FY07	FY08E	FY09E	FY10E
Operating Income	706	928	1,224	1,603
Other income	60	72	86	104
Total Expenditure	465	615	800	1,033
EBITDA	241	313	424	570
Depreciation	29	14	26	25
EBIT	272	370	485	649
Interest	0	0	0	0
Profit bef. Tax & ext. items	272	370	485	649
Extraordinary items	0	0	0	0
Provision for taxation	72	98	128	172
PAT	200	272	357	478

Balance Sheet (Rs. Mn)

(Year Ending Mar 31)	FY07	FY08E	FY09E	FY10E
Net worth	1,474	1,746	2,103	2,581
Secured loans	0	0	0	0
Deferred Tax	7	7	7	7
Minority Interest	0	0	0	0
Total Liabilities	1,482	1,754	2,111	2,588
Net Block	225	248	290	331
Capital Work in Progress	4	4	4	4
Goodwill on Consolidation	52	52	52	52
Investments	686	686	686	686
Net Current Assets	512	762	1,076	1,513
Total Assets	1,482	1,754	2,111	2,588

Valuation table

Y/E March 31 March	Total Revenues	Net profit	EPS (Rs)	ABV (Rs)	Core RoE (%)	RoE (%)	PE (x)	P/ABV (x)
FY2007	766	200	20.0	147.4	21.9	16.6	34.5	4.7
FY2008E	1,000	272	27.2	174.6	19.6	16.9	25.3	3.9
FY2009E	1,310	357	35.7	210.3	20.0	18.5	19.3	3.3
FY2010E	1,707	478	47.8	258.1	20.9	20.4	14.4	2.7

DISCLAIMER: This document is not for public distribution and has been furnished to you solely for your information and may not be reproduced or redistributed to any other person. The manner of circulation and distribution of this document may be restricted by law or regulation in certain countries, including the United States. Persons into whose possession this document may come are required to inform themselves of, and to observe, such restrictions. This material is for the personal information of the authorized recipient, and we are not soliciting any action based upon it. This report is not to be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. No person associated with Emkay Share & Stock Brokers Ltd is obligated to call or initiate contact with you for the purposes of elaborating or following up on the information contained in this document. The material is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon. Neither Emkay Share & Stock Brokers Ltd, nor any person connected with it, accepts any liability arising from the use of this document. The recipient of this material should rely on their own investigations and take their own professional advice. Opinions expressed are our current opinions as of the date appearing on this material only. While we endeavor to update on a reasonable basis the information discussed in this material, there may be regulatory, compliance, or other reasons that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. We and our affiliates, officers, directors, and employees world wide, including persons involved in the preparation or issuance of this material may; (a) from time to time, have long or short positions in, and buy or sell the securities thereof, of company (ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company (ies) discussed herein or may perform or seek to perform investment banking services for such company(ies) or act as advisor or lender / borrower to such company(ies) or have other potential conflict of interest with respect to any recommendation and related information and opinions. The same persons may have acted upon the information contained here. No part of this material may be duplicated in any form and/or redistributed without Emkay Share & Stock Brokers Ltd's prior written consent. No part of this document may be distributed in Canada or used by private customers in the United Kingdom. In so far as this report includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.

Emkay Share and Stock Brokers Ltd.,

Paragon Center, Ground Floor, C-6

Pandurang Budhkar Marg, Worli, Mumbai – 400 013. , Tel no. 66121212. Fax: 66121299