

Credit Analysis and Research Ltd. – CARE: “SUBSCRIBE”

4th December, 2012

CARE is a full service credit rating company in India and currently the second largest rating company in India in terms of rating turnover.

The Company's existing shareholders include domestic banks and financial institutions, such as IDBI Bank, Canara Bank, SBI and IL&FS, among others. It operates as a professionally managed company with a Board of Directors comprising a majority of independent directors.

At the upper end of the price band of Rs. 750, the Company is valued at 22x at its annualized H1FY13 annualized EPS of Rs. 17.43/-. Post Issue Market Capitalization/H1FY13 Annualized Sales stands at 1.03x seems reasonable. With due consideration to factors like a) established presence since 19 years, b) better operating margins as compared to its peers, c) freedom to enter newer markets, d) strong relationships with its clients, e) debt free company, f) cheaply valued as compared to listed peers like Crisil and ICRA. Hence, we recommend “SUBSCRIBE” to the issue.

Financial summary (Consolidated) - Rs. mn

Y/e 31 Mar (Rs. mn)	H1FY13	FY12	FY11#	FY10#
Total Operating Income	912	1,905	1,665	1,362
EBITDA Margin (%)	64.8	71.1	75.5	79.2
Reported PAT	498	1,158	879	857
PAT margin (%)	54.6	60.8	52.8	62.9
Equity Capital	285.53	285.53	95.18	95.18
Networth	4266.13	3768.38	2942.53	2134.95
RoNW (%)	11.67	30.72	29.89	40.14
Adjusted EPS on Post IPO equity	34.55**	40.55	30.80	30.01
P/E at Upper Price Band (x)	22	19	24	25

Source: RHP, Ajcon Research ** annualized EPS,

Note: EPS calculated on Post IPO Equity and FY11 and FY10 are standalone numbers whereas H1FY13 and FY12 are on consolidated basis

Note: IDBI Bank, Canara Bank, SBI, IL&FS, Federal Bank, IL&FS Trust (Equity shares held on behalf of Milestone Fund), Milestone Trusteeship (Equity Shares held on behalf of Milestone Army Trust), ING Vysya and Tata Investment are the selling shareholders in the offer for sale.

About the Business

The Company is a leading, full service credit rating company in India, and for the year ended March 31, 2012, it was the second largest rating company in India in terms of rating turnover. It has over 19 years of experience in rating debt instruments and related obligations covering a wide range of sectors, such as manufacturing, services, banks and infrastructure. It offers a wide range of rating and grading services across a diverse range of instruments and industries. In addition, provides general and customized industry research reports. Since incorporation in

Listing on	NSE and BSE	
IPO Issue date	December 07 – 11, 2012	
IPO Issue size	Rs. 5.04- 5.4 bn	
FV	Rs. 10	
Price Band	Rs. 700 - 750 per share	
Offer for sale	7.19 mn equity shares	
Lot size	20 Shares	
Equity shares post issue	16.66 mn equity shares	
Issue Structure	QIBs – 50% Retail – 35% Non Institutional Buyers – 15%	
IPO Grading	Exempted by SEBI from obtaining IPO grading for the offer	
Post issue market capitalization	Rs. 21.4 bn	
Book Running Lead Manager	Kotak, BoFA Merrill Lynch, Edelweiss, ICICI Securities, IDBI Capital and SBI Capital Markets	
Registrar to the issue	Bigshare Services Private Ltd.	
Shareholding Pattern (%)	Pre Issue	Post Issue
Promoters/FI	100	74.78
Public	-	25.22
Total	100	100

April 1993, it has completed 19,058 rating assignments and have rated Rs. 44,036.03 billion of debt as of September 30, 2012. The Company's list of clients includes banks and other financial institutions, private sector companies, central public sector undertakings, sub-sovereign entities, small and medium enterprises ("SMEs") and micro-finance institutions, among others. The Company has rating relationships with 4,644 clients as of September 30, 2012.

It is recognized by the Capital Markets Development Authority, Republic of Maldives to carry out ratings of debt instruments and bank loans and facilities in respect of Maldivian companies, through its office in the Republic of Maldives, and it is focused on expanding its ratings business in other countries, including Nepal and Mauritius, where it intends to provide rating services through joint ventures in the future.

The Company has also been recognized by Bank of Mauritius for using its ratings for risk weighting of bank claims on corporates for capital adequacy purposes. The Company has also been granted indirect recognition by the Hong Kong Monetary Authority as an external credit assessment institution for the purposes of the regulatory capital framework in Hong Kong. Authorized institutions incorporated in Hong Kong are now permitted to use a rating by the Company for determining the capital requirements for credit exposure to Indian corporates. The Company is exploring opportunities to provide risk management solutions and training in risk management practices to banks and financial institutions in Nigeria pursuant to an exclusive memorandum of understanding with Riskmap Consulting Limited, a Nigerian risk management consulting company.

The Company has entered into a non-binding memorandum of understanding with four credit rating agencies, each located in Brazil, Portugal, Malaysia and South Africa, to establish an international credit rating agency, which would provide international scale ratings to assist local issuers in mobilizing resources from international financial markets. The Company has received a no objection letter from SEBI to enter into a joint venture for the establishment of an international credit rating agency, subject to satisfaction of certain conditions mentioned therein.

Objects of the issue

To carry out sale of 7,199,700 equity shares by the selling shareholders and to achieve benefits of listing on stock exchanges.

Key Strengths

Established presence in rating debt instruments and bank loans and facilities

CARE has over 19 years of experience in rating debt instruments and related obligations covering a wide range of sectors, and as of September 30, 2012, it had rating relationships with 4,644 clients. CARE believes it is well equipped to rate most kinds of short, medium and long-term debt instruments, such as commercial paper, bonds, debentures, preference shares and structured debt instruments; bank loans and facilities, both fund-based and non fund-based; and deposit obligations, such as inter-corporate deposits, fixed deposits and certificates of deposit. The experience and knowledge that it has gained over the years, along with its planning and execution strategies, enables it to retain its current client base and explore new opportunities that emerge in the industry.

The Company's main rating product is rating of debt instruments and bank loans and facilities, which provides it with higher volumes than other products. The Company has a significant rating coverage of Indian banks and financial institutions.

It has achieved steady growth in its ratings business. The total number of debt instruments it rated increased from 3,934 as of March 31, 2008 to 14,524 as of March 31, 2012, at a CAGR of 38.6% during such period. The total number of debt instruments it rated as of September 30, 2012 was 17,237. The volume of debt rated by the Company increased from Rs. 4,325.84 billion as of March 31, 2008 to Rs. 9,268.61 billion as of March 31, 2012, at a CAGR of 21.0% during such period. The volume of debt rated by CARE as of September 30, 2012 stood at Rs. 3,571.20 billion.

Domain experience across a range of sectors

The Company has rated debt instruments covering a diverse range of sectors, such as manufacturing, services, banks and infrastructure. The Company also has experience in providing debt and issuer ratings to many types of enterprises, including corporates, banks, financial institutions, public sector undertakings, state government undertakings, sub-sovereign entities, NBFCs, SMEs and micro-finance institutions. CARE believes that it is able to cover a range of sectors because its ratings business is supported by a strong team of skilled analysts and support staff. The Company's analysts are predominantly post-graduate professionals, such as MBAs and other finance professionals with engineering or economics backgrounds, as well as chartered accountants, economists and chartered financial analysts. The Company's research team provides in-house support to its ratings team in the form of in-depth industry knowledge over a range of sectors. ITS research team comprises analysts having varied experience across sectors. Its ability to provide rating services across a diverse range of sectors is on account of CARE's 19 years of rating experience, backed by the in-depth sectoral knowledge gained by its research team over the years.

Strong rating credibility and brand presence

CARE believes that its brand represents a high level of rating credibility, as its ratings display high ordinality. In order for ratings to be used as a reliable indicator of credit risk, it is believed that it is critical for a rating agency to demonstrate, over a period of time, strong correlation between the actual performance of the rating it assigns and what the rating itself conveys. Since 2007, CARE has published default and transition studies evaluating the performance of ratings, with its most recent default and transition study published in 2012 covering the nine year period from March 31, 2003 to March 31, 2012. The Company believes that the ratings assigned by it show that a higher category of rating demonstrates a relatively lower likelihood of default and a higher degree of stability.

CARE believes that the reliability of the ratings is underpinned by the established rating procedures that its analysts use and the quality control systems and procedures employed by a separate quality control department. Its quality control department ensures that robust quality checks are in place for all ratings and are in compliance with the applicable laws in India, including the CRA Regulations. CARE follows a standardized and comprehensive rating process, which is also subject to operational audits as prescribed by SEBI. In addition, it has an internal rating committee comprising senior executives from the Company and an external rating committee comprising a majority of independent members. The rating committees are the final authorities for assigning ratings on behalf of the Company. The Company believes that it has strong brand recognition and credibility in the ratings market, gained through years of experience in the ratings business. The credibility of its ratings is also reflected in the fact that it has received certifications and accreditations from various regulatory bodies and entities.

Strong origination capabilities and relationship management

The Company has a strong and widespread business development team across multiple cities in India. CARE's list of clients includes banks and other financial institutions, private sector companies, central public sector undertakings, sub-sovereign entities, SMEs and micro-finance institutions, among others. It had ratings relationships with 4,644 clients as of September 30,

2012. Its origination capabilities are further supported by its business development teams, which collate the ideas and views of various market participants, regulators and policy makers and pass them on to the product development team for further study and implementation. We believe that we have a stable and esteemed core client base representing most of the major Indian industrial groups, banks and conglomerates. Further, CARE believes that its strong brand and 19 years of experience in the ratings business enables us not only to obtain repeat business from its existing clients, but to source new business as well.

Key Concerns

SME rating, in which CARE plans to increase its focus, is a relatively low margin business.

State of the economy has an impact on the number of debt / IPO issues, which is out of company's control.

Ratings business is largely dependent on brand recognition and reputation. An adverse event like the global economic slump of 2008-09 raised question mark on the credibility of rating agencies.

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