

STOCK IDEA  
Rating: BUYIndian Railway Finance Corp Ltd  
NBFC

Indian Railway Finance Corporation (IRFC), incorporated in 1986 is a GoI undertaking and a Schedule 'A' Public sector enterprise under the purview of Ministry of Railways (MoR). The promoter of the company is the President of India (holding ~86% stake and acting through the MoR). The company got listed on the NSE / BSE on January 29, 2021. IRFC is registered as (NBFC – ND-SI) and (NBFC- IFC) with RBI. Their principal business is to borrow funds from the financial markets to finance the acquisition / creation of assets which are then leased out to the Indian Railways (IR). The funds are utilized for acquiring rolling stock assets and also building up infrastructure, constituting significant part of annual capital expenditure of IR. A major portion of IRFC's revenue is generated from the leasing of rolling stock assets, comprising locomotives, passenger coaches and freight wagons, to the IR. As of Dec 30, 2020, the company's total AUM consisted of 53.6% of lease receivables primarily in relation to Rolling Stock Assets and 44.3% of advances against leasing of Project Assets, 2.1% of loans to central public sector enterprises entities (RVNL & IRCON) under the administrative control of MoR

## INVESTMENT RATIONALE

## Capacity expansion in Railway Sector to boost growth

IRFC has played a strategic role in financing the operations of the Indian railways which constitutes a crucial part of India's infrastructure. In FY20, IRFC financed Rs. 71,392 Cr accounting for 48.2% of the actual capital expenditure of the Indian Railways. The Union Budget proposed a capital expenditure of ₹ 1,610 billion for the Indian Railways for Fiscal 2021, which was higher than the capital expenditure of ₹ 1,480.64 billion in Fiscal 2020. The National Railway plan 2030 has mandated a capex of around INR 10 lakh crore. This will involve significant financing which will directly benefit IRFC as it is primary financing source for the Indian Railways. To further expand its funding horizon, IRFC also plans to diversify its business profile by lending outside Indian Railways.

## Regulatory arbitrage providing high flexibility for business

As a NBFC, IRFC does not have to comply with RBI regulatory requirement on asset classification, income recognition, provisioning to the extent of exposure to MoR. As a result IRFC has a strong asset quality, with a history of zero non-performing asset. The company is adequately capitalized with Tier – 1 capital of 434% of total risk weighted assets (as compared to mandated 15% CRAR) indicating high solvency. The high CRAR is mainly on account of the company's ~98% exposure to MoR which is considered risk free and the only risk weighted assets in the AUM pertains to RVNL and IRCON, which is 2% of the portfolio.

## Monopolistic, Stable and Low Risk business Model

IRFC enjoys monopoly in its business having a credible moat as it finances ~48% of the railway capital outlay. IRFC generates stable earnings due to dependence on financing the Indian Railways and government capex on national carrier. The expenses incurred by IRFC with respect to any foreign currency hedging costs and/ or losses (and gains, if any) as well as any hedging costs for interest rate fluctuations are built into the weighted average cost of incremental borrowing. Risk relating to damage to Rolling stock assets as a result of natural calamities and accidents are passed onto the MoR. IRFC manages its cash flows through an active asset and liability management strategy. Its asset-liability management model is structured in a manner which ensures that it has minimum asset-liability mismatches. It borrows on a long-term basis to align with the long-term tenure of the assets funded by it.

## High operational efficiency driving increased profitability

IRFC's total revenue from operations increased at a CAGR of 21% over FY18-20 to INR 13,421 Cr driven by strong growth in AUM (~27% CAGR) while net profit grew 26% to INR 3,192 Cr over the same period. The company is cost efficient (Cost to income: 2.94%) with moderate margins (NIM: 1.38%). Low overhead and administrative cost and high operational efficiency has resulted in increased profitability. The employee expenses have accounted at an average of 0.05% of the total income. Furthermore, even though the company is governed under normal taxation, however there is no tax liability as the unabsorbed depreciation is more than the net taxable income. IRFC is also exempt from GST applicability on leasing of rolling stock assets. IRFC also enjoys competitive cost of borrowings which was ~7.37% in FY20 which has come down to 6.4% in 9MFY21 based on strong credit rating (AAA ratings from both domestic and international rating agencies) received by the company

## Valuation and Outlook:

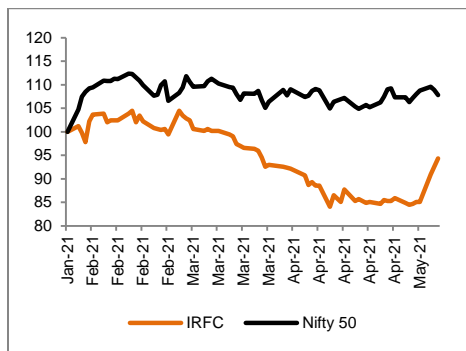
IRFC's growth is highly dependent on MoR's expansion plans for Indian railways. With the expansion of the freight network and passengers demand, the requirement of rolling stock is expected to grow substantially. This will in turn increase AUM which majorly consists of lease receivables primarily in relation to Rolling stock assets (~55%). With a Railway vision plan of 2030 on track, IRFC is all set to explore new horizons. Key Risk is substantial dependence on IR for revenue which may lead to risk of MoR raising funds directly from banks and other financial institutions. The offloading of ~11% in the next three years to maintain 25% minimum public shareholding as per SEBI norms, also remains an overhang on the share price. Favorable asset quality owing to zero NPA, strong financial flexibility, and low credit risk profile augurs well for the company. Given that the Cost of Borrowing is expected to decline from FY21 onwards, we expect NIM ratio to improve. The company is currently trading at a P/BV of 0.9x. By applying a P/BV of 0.86x on FY23E BV, we arrive at a target price of Rs. 28 per share which is an upside of 21.5% to CMP. Hence, we recommend a 'BUY' on the shares of IRFC Ltd.

Date	18-May-21
CMP	INR 23
Target Price	INR 28
Potential Upside	21.5%

Market Data	
O/S Shares (In Cr)	1307
Equity Cap (INR Cr)	13,068
Mkt Cap (INR Cr)	30,188
52 Wk H/L (INR)	26.6/20.7
3M Volume Avg ('000)	23,290
Face Value	10
Bloomberg Code	IRFC IN

BSE Sensex	50,193
NSE Nifty	15,108

## Comparative Price Chart



Particulars	Mar 21	Jan 21
Promoters	86.36%	86.36%
FII	1.44%	2.23%
DII	4.23%	3.11%
Others	7.97%	8.30%

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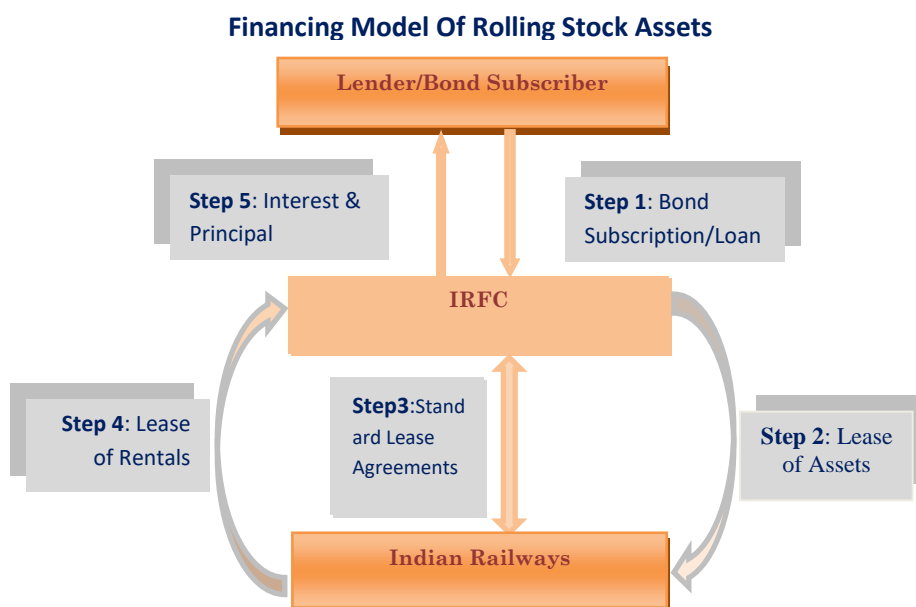
## Key Financials

Particulars (INR Mn)	Total Income	Net Interest Inc	NIM (%)	PAT	EPS (INR)	P/BV (x)
FY23E	170,711	55,883	1.7%	54,992	4.2	0.64
FY22E	155,193	46,350	1.5%	45,539	3.5	0.73
FY21E	144,793	41,133	1.4%	40,395	3.1	0.82
FY20	134,211	32,584	1.4%	31,921	3.4	0.86
FY19	109,874	28,043	1.5%	21,399	3.3	0.83

In FY20, IRFC was entitled to a margin of 40 bps over weighted average cost of borrowing for leasing of Rolling stock assets.

**Company Snapshot:** IRFC is a dedicated market borrowing arm of the Indian Railways with the government holding ~86% stake. They are registered with the Reserve Bank of India as a NBFC. Its primary business is financing the acquisition of rolling stock assets, which includes both powered and unpowered vehicles, for example locomotives, coaches, wagons, trucks, flats, electric multiple units, containers, cranes, trollies and other items of rolling stock components (collectively, "Rolling Stock Assets"), leasing of railway infrastructure assets and national projects of the Government of India (collectively, "Project Assets") and lending to other entities under the Ministry of Railways, Government of India (MoR). The MoR is responsible for the procurement of Rolling Stock Assets and for the improvement, expansion and maintenance of Project Assets while IRFC is responsible for raising the finance necessary for such activities. Over the last three decades, the company has played a significant role in supporting the capacity enhancement of the Indian Railways by financing a proportion of its annual plan outlay and forms a core source of funding having a contribution of 48% of the total funding for Indian Railways

Over last four years, IRFC was responsible for financing an average of 81% of Indian Railway's total Rolling Stock Assets



Source: Systematix Research, Company Filings

**IRFC follows a financial leasing model for financing its Rolling stock assets which comprises 53.6% of AUM**

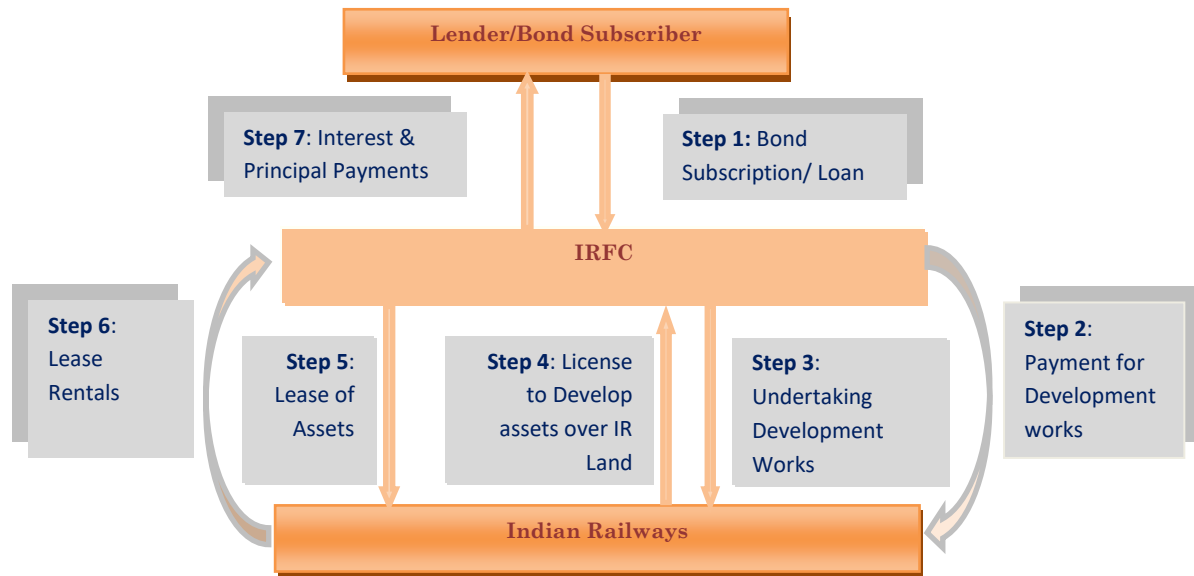
<b>Lease Period</b>	IRFC is following Financial Leasing Model with a lease period of 30 years (primary period & secondary period of 15 years each), During the primary and secondary lease periods, the full value of assets, including interest, has been recovered from the MoR. On completion of lease agreement, assets are transferred to MoR at nominal price.
<b>Sources of Funds</b>	At the beginning of each Fiscal, the MoR provides IRFC with its target fund requirement based on its planned capital expenditure, which IRFC meet by raising funds through various sources including the issue of taxable and tax-free bonds in India, term loans from banks/ financial institutions, external commercial borrowings including bonds and syndicated loans, internal accruals, asset securitization and lease financing.
<b>Standard Lease Agreement</b>	Every year, IRFC enters into a Standard Lease Agreement with MoR. Lease rentals include the value of the Rolling Stock Assets leased by IRFC to the MoR in the relevant fiscal year +the weighted average cost of borrowing +a certain margin, all in accordance with the terms of the Standard Lease Agreement.
<b>Margin</b>	In FY20, IRFC was entitled to a spread of 40 bps over weighted average cost of borrowing

Diversified sources of funding, credit ratings and strategic relationship with the MoR, have enabled IRFC to keep costs of borrowing competitive.

The company's overall AUM was at Rs 2.97 lakh crore as on Dec 31, 2020 and expected to grow on the back of National Vision plan.

Major source of funding for IRFC is through issuance of long term taxable bonds comprising ~47% of total funding

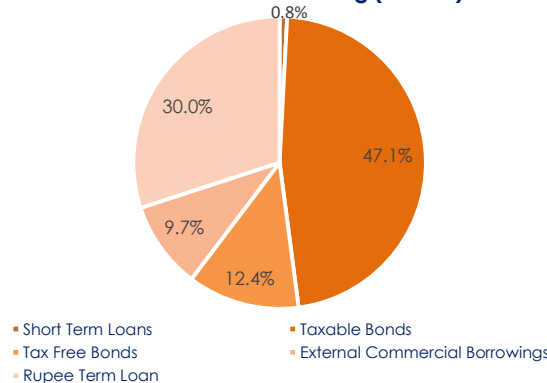
Financing Model Of Project Assets



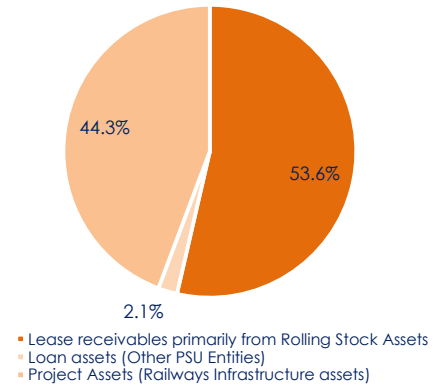
Source: Systematix Research, Company Filings

IRFC follows a financial leasing model for financing its Project Assets which comprises 44.29% of AUM	
<b>Standard Lease Agreement</b>	IRFC acquires leasehold interest in the project assets under a lease agreement and MoR is required to pay lease rentals. The company has leased out infrastructure assets such as doubling projects and electrification projects through a licensing agreement with MoR. The primary lease period is for 15 years and the secondary lease period commences from the date next to the expiry of the primary lease for 15 years. The lease rental shall be paid in annual installments on October 15 of every year.
<b>Margin</b>	In FY20, IRFC was entitled to a spread of 35 bps over weighted average cost of borrowing.

Diversified Sources of Funding (Dec 20)



AUM Break-Up (Dec 20)



Source: Systematix Research, Company Filings

IRFC's funding requirements are sourced through diverse sources including the issue of taxable and tax-free bonds in India, term loans from banks/financial institutions, external commercial borrowings including bonds and syndicated loans, internal accruals, asset securitization and lease financing. IRFC's Cost of Borrowings was 6.97%, 6.82%, 7.09% and 7.27% in Fiscals 2017, 2018, 2019 and 2020 respectively.

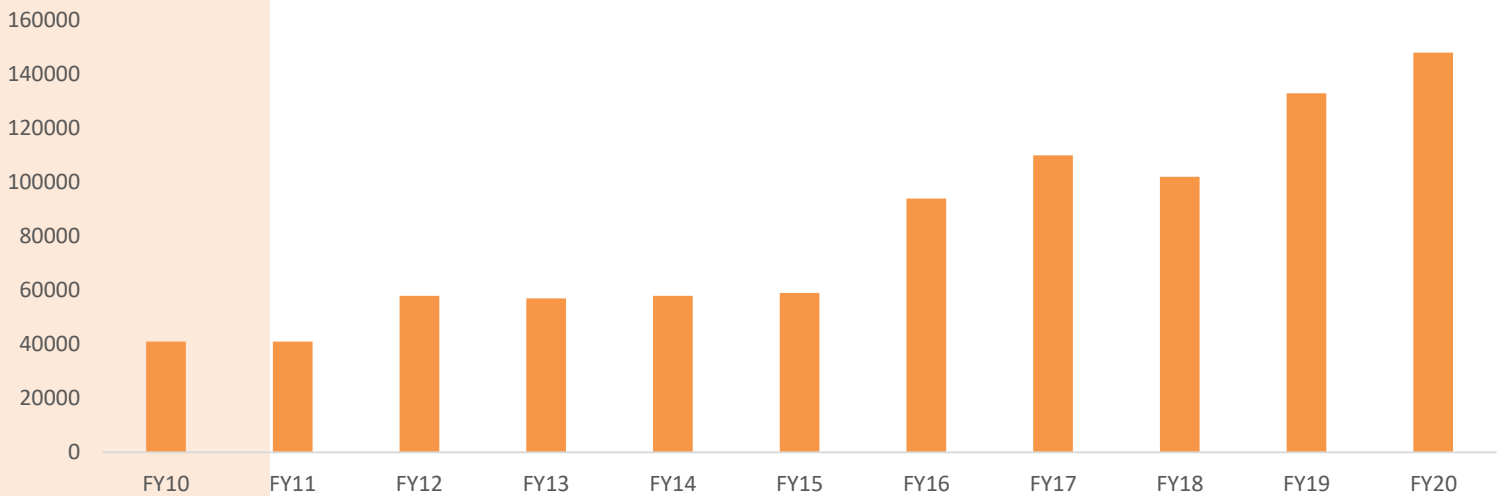
IRFC's AUM represents sum of total lease receivables, loans to Other PSU Entities, and advances against leasing of Project Assets. The company's overall asset under management (AUM) was at Rs 2.97 lakh crore as on 31st Dec, 2020 which has grown at a CAGR of 27% over FY18-20. IRFC expects its AUM to reach Rs.3.5 Lakh Crores in FY22 as they are planning to participate in Rail Vision Plan.

**Railway capex noted a growth of 20% CAGR post FY15 compared to 14% CAGR in the preceding ten years**

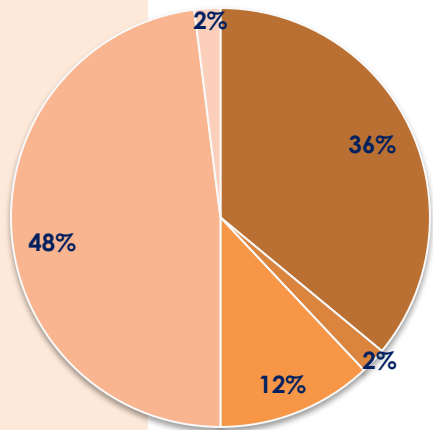
## Capacity expansion in Railway Sector to boost growth

Railway capital expenditure has attained a considerable pickup post FY15. Railway capex noted a growth of 20% CAGR post FY15 compared to 14% CAGR in the preceding ten years. Railway capex is expected to continue to grow at the robust pace witnessed in recent years on the back of various initiatives like – network decongestion and expansion, electrification, DFC - dedicated freight corridors, high speed railways (bullet train between Mumbai-Ahmedabad), elevated corridors and addition of rolling stock. The primary sources of funds for the planned capital outlay of the Indian Railways are GBS, internally generated funds, public private partnerships and market borrowings leasing through IRFC and other sources (EBR-IF), railway safety fund and RRSK. With the expansion of the freight network and passengers demand, the requirement of rolling stock will increase substantially. Over last four years, IRFC was responsible for financing an average of 81% of Indian Railway's total Rolling Stock Assets

## Railways Capex (INR Cr) has attained significant momentum post FY15

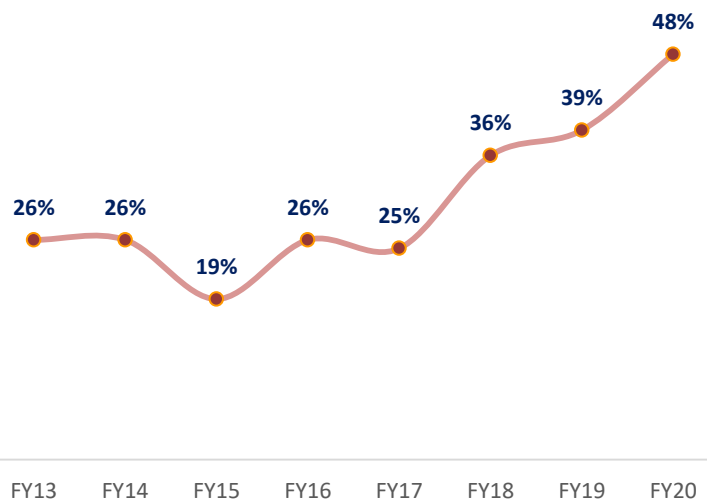


### IRFC contribution of 48% of the total funding for Indian Railways



- Budgetary Support
- Internal Resources
- Rail Sanraksha
- Borrowings from IRFC
- Borrowings from others

### Rising Share of IRFC in Railway capex Funding

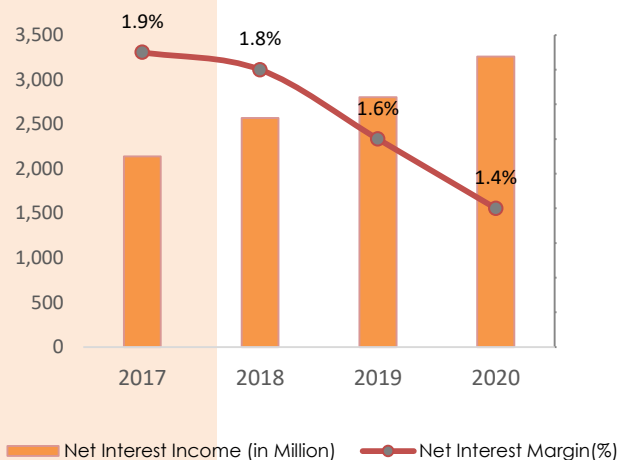


Source: Systematix Research, Company Filings

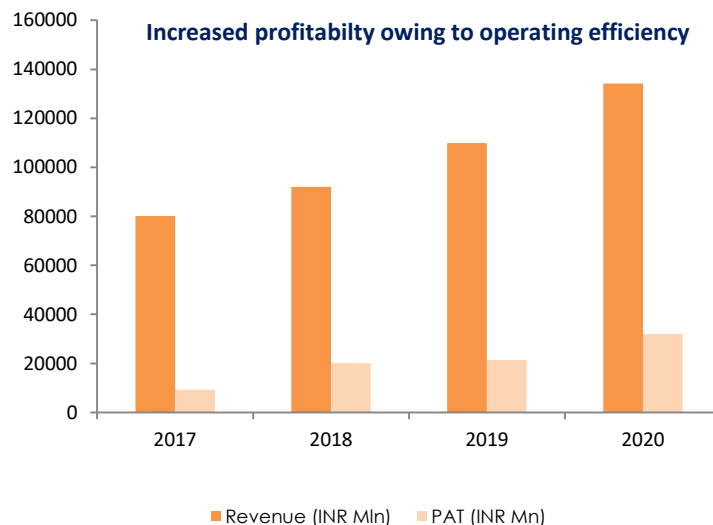
IRFC has played a significant role in supporting the capacity enhancement of the Indian Railways by financing a significant proportion of its annual plan outlay. IRFC is having a contribution of 48% i.e. Rs. 71,392 crores of the total funding for Indian Railways (i.e. Rs. 1.48 Lac Cr) for FY2020. The extensive expansion plans of the Indian Railways in the future will involve significant financing, and as a primary financing source for the Indian Railways, the IRFC's operations will increase significantly. The share of IRFC has grown from 19% in FY15 to 48% in FY20.

## Financial Analysis

**NIM expected to rise owing to reduced cost of borrowings**



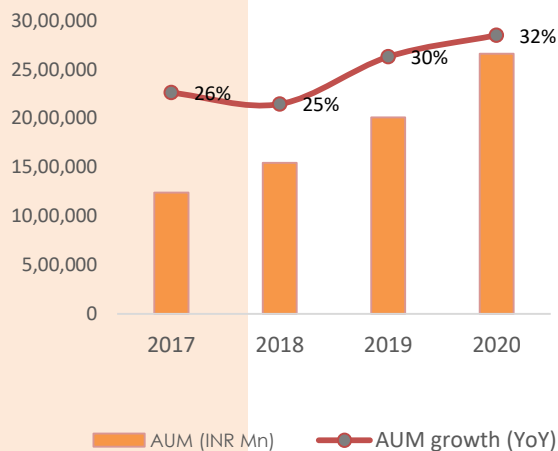
**Increased profitability owing to operating efficiency**



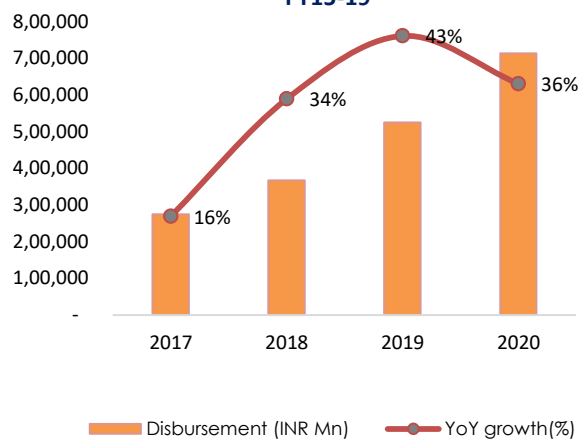
Source: Systematix Research, Company Filings

IRFC has demonstrated consistent growth in terms of funding and profitability. Company's revenues arise from Lease Income, Dividend Income and Interest on lease advance, loans, deposits and investments. Its total revenue from operations increased by 19% from Rs. 92,078 million in Fiscal 2018 to Rs. 1,09,874 million in Fiscal 2019 and by 22% to Rs. 1,34,211 million in Fiscal 2020. Lease Income consists around 80-85% of Total Revenue Income. IRFC's low overhead and administrative costs and high operational efficiency has resulted in increased profitability. IRFC is having 24 permanent employees as of FY20. IRFC's employee benefit expenses were 29.95 million, 55.26 million, 62.51 million and 62.65 million in Fiscal 2017, 2018, 2019 and 2020 respectively and accounted for 0.03%, 0.06%, 0.06% and 0.05% of total income, respectively, in such periods.

**AUM has grown at a CAGR of 27% over FY18-20**



**Disbursements have grown at 45% CAGR over FY15-19**



Source: Systematix Research, Company Filings

As of December 30, 2020, total AUM, consisted of 55.34% of lease receivables primarily in relation to Rolling Stock Assets, 2.25% of loans to Other PSU Entities, and 42.41% of advances against leasing of Project Assets. IRFC expects AUM to reach INR 3.5 lakh crore by FY22.

IRFC disbursements grew at 45% CAGR over FY15-20 while its contribution in railway capex increased from 19% to 48% over the same period. In addition to raising funds for the Indian Railways, IRFC have also disbursed loans amounting to INR 14,709 million and INR 7,000 million to a central public sector enterprise in Fiscal 2019 and the six months ended September 30, 2019, respectively

*As compared to other NBFCs, IRFC enjoys zero non-performing asset owing to exemption from exposure norms*

*President of India holds ~86% stake in IRFC post listing on 29<sup>th</sup> January 21.*

*Among Institutional holdings, HDFC Trustee Co Ltd holds 1.46% stake, Insurance companies hold 1.18% stake and FPI hold 1.44% stake.*

### Peer Comparison

Key Parameters -FY20 (%)	PFC	REC	IRFC
NIM	3.2%	3.7%	1.4%
GNPA	7.4%	6.6%	0.0%
Cost to Income	13.0%	6.0%	2.9%

Source: Systematix Research, Company Filings

IRFC does not have to comply with RBI regulatory requirement on asset classification, income recognition, provisioning to the extent of exposure to MoR. As a result IRFC has a strong asset quality, with a history of zero non-performing asset. The NIM is expected to rise as cost of borrowings is expected to decline going forward. The cost to income ratio is also the lowest on the back of Low overhead and administrative cost.

### Details of Management

Name & Designation	Brief profile of Management
<b>Amitabh Banerjee</b> <b>Chairman &amp; Managing Director</b>	Mr. Amitabh Banerjee took over the charge on the IRFC Board on 21st May, 2020. He belongs to the IRAS Cadre of 1988 Civil Service Exam Batch. Prior to joining IRFC, he has been working in the capacity of Director Finance, Konkan Railway Corporation Limited (KRCL), he worked in the capacity of Director Finance in Hindustan Paper Corporation Limited (HPC) for 3 years. He has held several portfolios in the Finance Department of Ministry of Railways since 1989 through 2003, handling major projects like Gauge Conversion, Laying of New Lines, Track Doubling, Construction of Railway Bridges, etc.
<b>Shelly Verma</b> <b>Director (Finance) and CFO</b>	Shelly Verma is member of the Institute of Chartered Accountants of India. More than 30 years' experience in Power Sector Financing. Prior to her appointment to the Board of our Company, She has served in various capacities, including, most recently, as Executive Director (Finance) with the Power Finance Corporation Limited.
<b>Baldeo Purushartha</b> <b>Part-time Government Director</b>	Baldeo Purushartha is a Part-time Government Director of our Company. He is an IAS officer and a Joint Secretary at the Department of Economic Affairs, Ministry of Finance, Gol. He holds a bachelor's degree and a master's degree in history, from the University of Delhi. He is on the board of several institutions, including the India Infrastructure Finance Company Limited, ONGC Videsh Limited, Indian Railway Stations Development Corporation Limited and Asian Infrastructure Investment Bank
<b>Ashok Kumar Singhal</b> <b>Independent Director</b>	Ashok Kumar Singhal has been appointed as part-time Non-Official Independent Director on the Board of IRFC on 20th July, 2018. Shri Singhal carries with him rich and varied experience in Finance, Accounts, Law & Costing for a period spanning more than thirty five (35) years. He has worked with Ministry of Finance, Ministry of Defence, Ministry of Chemical & Fertilizers, and Department of Health & Family Welfare. He has done his M.Sc. (Finance) from University of Strathclyde, Glasgow, United Kingdom, L.L.B. from Agra University and is a member of Institute of Chartered Accountant



## Income Statement

Particulars (INR Mn)	FY 19	FY 20	FY 21E	FY 22E	FY 23E
Total Interest Income	109,874	134,210	144,792	155,192	170,711
Total Interest Expended	81,831	101,627	103,659	108,842	114,828
<b>Net Interest Income (NII)</b>	<b>28,043</b>	<b>32,584</b>	<b>41,133</b>	<b>46,350</b>	<b>55,883</b>
Non Interest Income	0	1	1	1	0
<b>Total Income</b>	<b>28,043</b>	<b>32,584</b>	<b>41,134</b>	<b>46,351</b>	<b>55,883</b>
<b>Total expenditure</b>	<b>214</b>	<b>642</b>	<b>738</b>	<b>791</b>	<b>871</b>
Employee cost	63	63	72	78	85
Other expenses	152	579	666	714	785
<b>Profit before Provision</b>	<b>27,829</b>	<b>31,942</b>	<b>40,395</b>	<b>45,559</b>	<b>55,012</b>
Provision (Impairment on Financial Instruments)	275	21	0	20	20
<b>Profit before Tax</b>	<b>27,553</b>	<b>31,921</b>	<b>40,395</b>	<b>45,539</b>	<b>54,992</b>
<b>Tax expense/(credit)</b>	<b>6,154</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>PAT</b>	<b>21,399</b>	<b>31,921</b>	<b>40,395</b>	<b>45,539</b>	<b>54,992</b>
<b>EPS</b>	<b>3.3</b>	<b>3.4</b>	<b>3.1</b>	<b>3.5</b>	<b>4.2</b>

Source: Systematix Research, Company Filings

## Cash Flow Statement

Particulars (INR Mn)	FY19	FY20	FY21E	FY22E	FY23E
Net Cash Generated From Operations	(417,482)	(627,176)	(125,396)	(152,704)	(258,181)
Net Cash Flow from/(used in) Investing Activities	13	15	(3)	(3)	(3)
Net Cash Flow from Financing Activities	417,495	627,138	125,487	152,958	258,260
Net Inc/Dec in cash equivalents	26	(23)	88	250	75
Opening Balance	11	37	14	102	352
Closing Balance Cash and Cash Equivalents	37	14	102	352	427

Source: Systematix Research, Company Filings

## Key Ratios

Key Ratio	FY19	FY20	FY21E	FY22E	FY23E
NIM (%)	1.5%	1.4%	1.4%	1.5%	1.7%
BVPS (INR)	26.51	25.50	26.99	30.27	34.22
P/B (x)	0.83	0.86	0.82	0.73	0.64
RoE (%)	8.6%	10.5%	11.5%	11.5%	12.3%
EPS (INR)	3.3	3.4	3.1	3.5	4.2

Source: Systematix Research, Company Filings

## Balance Sheet

Particulars (INR Mn)	FY19	FY20	FY21E	FY22E	FY23E
<b>Non-current assets</b>					
Property, plant and equipment	112	110	111	112	112
Derivative Financial Instrument	467	0	0	0	0
Loans	58,955	64,234	72,396	38,798	42,678
Current tax assets (Net)	415	6,308	6,308	6,308	6,308
Other non-financial assets	14,987	14,725	8,688	7,760	8,536
<b>Total non-current assets</b>	<b>74,936</b>	<b>85,378</b>	<b>87,504</b>	<b>52,978</b>	<b>57,635</b>
Current assets					
Financial assets					
Lease Receivable	1,250,265	1,485,798	1,692,975	2,072,248	1,927,425
Cash and cash equivalents	37	14	102	352	427
Bank balances other than (iii) above	774	994	994	994	994
Investments	131	115	115	115	115
Other financial assets	738,239	1,182,743	1,139,520	998,201	1,457,532
<b>Total current assets</b>	<b>1,989,447</b>	<b>2,669,663</b>	<b>2,833,705</b>	<b>3,071,910</b>	<b>3,386,492</b>
<b>TOTAL ASSETS</b>	<b>2,064,383</b>	<b>2,755,041</b>	<b>2,921,209</b>	<b>3,124,889</b>	<b>3,444,127</b>
<b>EQUITY AND LIABILITIES</b>					
<b>Equity</b>					
Equity share capital	93,805	118,805	130,685	130,685	130,685
Other equity	154,858	184,193	222,057	264,864	316,557
<b>Total equity</b>	<b>248,663</b>	<b>302,998</b>	352,742	395,549	447,242
<b>Liabilities</b>					
<b>Non-current liabilities</b>					
Borrowings	503,348	790,863	778,451	871,865	959,051
Other financial liabilities	72,999	103,374	103,659	108,842	114,828
Debt Securities	1,235,979	1,552,905	1,681,454	1,743,730	1,918,103
Derivative Financial Instrument	3,106	4,065	4,065	4,065	4,065
Other non-financial liabilities	48	322	322	322	322
<b>Total non-current liabilities</b>	<b>1,815,480</b>	<b>2,451,528</b>	<b>2,567,951</b>	<b>2,728,824</b>	<b>2,996,370</b>
<b>Current liabilities</b>					
Financial liabilities					
Trade payables	122	378	378	378	378
Provisions	118	138	138	138	138
<b>Total current liabilities</b>	<b>240</b>	<b>516</b>	<b>516</b>	<b>516</b>	<b>516</b>
<b>Total liabilities</b>	<b>1,815,720</b>	<b>2,452,044</b>	<b>2,568,466</b>	<b>2,729,339</b>	<b>2,996,885</b>
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>2,064,383</b>	<b>2,755,041</b>	<b>2,921,209</b>	<b>3,124,889</b>	<b>3,444,127</b>

Source: Systematix Research, Company filings



**DISCLOSURES/APPENDIX****ANALYST CERTIFICATION**

I/We, **CA Liza Fernandes**, hereby certify that (1) views expressed in this research report accurately reflect my/our personal views about any or all of the subject securities or issuers referred to in this research report, (2) no part of my/our compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed in this research report by Systematix Shares and Stocks (India) Limited (SSSIL) or its group/associate companies, (3) reasonable care is taken to achieve and maintain independence and objectivity in making any recommendations.

Disclosure of Interest Statement	Update
Analyst holding in the stock (%)	None
Served as an officer, director or employee	No

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