ICRA
A MOODY'S INVESTORS SERVICE COMPANY

INDIAN BANK BROKERAGE INDUSTRY

Bank brokerage: Riding the retail investor wave

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ICRA's outlook on the bank brokerage industry is stable

Despite stiff competition from discount brokerage houses, the bank brokerage companies have delivered healthy metrics. Going forward, bank brokerages are expected to increase the share of non-broking sources of income

Stable outlook on bank brokerage industry

The outlook for the bank brokerage industry is stable. ICRA expects bank brokerages to continue to build their retail franchise and focus more on technology and digital models for customer acquisition. Supported by these factors, bank brokerages are expected to register a healthy growth in client addition as well as transaction volumes, though their share in total active clients would moderate owing to the rapid expansion of the discount broking model. The blended yields are expected to compress going forward, though the focus on fee and fund-based income would support the profitability. Bank brokerages are expected to continue to enjoy better brand recall, trust, higher credibility and financial flexibility by virtue of being a part of banking groups and would, therefore, remain a prominent part of the industry value chain.

ICRA expects the net operating income (NOI) of bank brokerages to grow 20-25% year-on-year (YoY) in FY2022 supported by steady broking income along with an uptick in the margin funding and distribution businesses; the ramp-up of other capital markets related businesses could further support the earnings profile. The net profit for bank brokerages is expected to grow 17-20% during the same period. The borrowings levels of bank brokerages are expected to increase in the current fiscal to support their margin funding business. ICRA expects the gearing levels of bank brokerages to be in the range of 1.5-2 times in FY2022 (Gearing across entities to vary from 1-3 times based on the scale of margin funding operations).

- **Bank brokerages deliver strong performance:** Despite facing stiff competition from discount brokerage houses, bank brokerage companies have delivered healthy metrics. The pool of ICRA-rated bank brokerages reported a strong performance in FY2021 with the estimated average daily turnover (ADTO) increasing 28% YoY to Rs. 1.51 lakh crore from Rs. 1.18 lakh crore in FY2020, led by the healthy growth in the retail derivates segment. Despite the changes in the margin requirements, the performance remained healthy in Q1 FY2022 with an estimated ADTO of Rs. 1.64 lakh crore, driven by favourable retail investor sentiment. However, the market share of the sample pool of ICRA-rated bank brokerages in terms of transaction volumes declined in FY2021 and moderated further in Q1 FY2022 as they continue to lose share to discount brokers. Nevertheless, the NOI reported a healthy increase.
- **Broking income remains primary income contributor:** Broking income continues to be the major source of income for bank brokerage companies, accounting for 55% of the total revenue in FY2021 compared to 48% in FY2020 and 46% in FY2017. ICRA's sample pool of five bank brokerages reported a robust growth in the total revenue in FY2021, up 44% YoY. The cost structure and operational efficiency of the bank brokerage companies also improved over the past few years with focus on the rationalisation of branches coupled with cautious efforts

ICRA estimates discount brokerage houses accounted for nearly half of the active clients on NSE

towards the transition to a digital business model, thereby improving the operational efficiency across brokerages. ICRA's sample pool of five bank brokerages reported an all-time high net profit of Rs. 3,246 crore in FY2021, up 79% YoY.

- **Non-broking revenue pie expected to surge:** Going forward, the bank brokerages are expected to increase the share of non-broking sources of income, namely capital market lending business, distribution income and investment banking revenue. Further, the capital market related lending business (margin trade funding (MTF), employee stock option plan (ESOP) funding, distribution and others) witnessed a significant ramp-up in recent years owing to higher funding requirements on the back of higher trading volumes, which increased the gross gearing to 0.6 times as of March 2021 from 0.3 times as of March 2020, which is primarily funded through commercial papers.
- **Growing prominence of discount brokerage houses; increasing consolidation:** Over the past five years, discount brokerages houses have cemented their positions and emerged as prominent market participants. The market share of discount brokerages in terms of National Stock Exchange (NSE) active clients increased to 49% as of August 2021 from 2% as of March 2016. On the other hand, bank brokers, which held a market share of over ~33% as of March 2016, witnessed a sharp decline in their market share during the last few fiscals, to ~20% as of August 2021. The share of traditional brokers in total active clients contracted to 30% from 65% during the same period. However, the total NSE active client base has expanded to 240.9 lakh as of August 2021 from 47.4 lakh as of March 2016 with discount brokerages taking an estimated 56% of the incremental pie, followed by traditional brokers at 24% and bank brokers at 19%. As of August 2021, three of the top five brokerages in terms of active clients were discount brokerages compared to nil as of March 2016.
- **Strong performance of Indian capital markets:** The Indian capital markets reported a stellar performance in FY2021 despite the concerns regarding the Covid-19 pandemic. The ADTO increased to Rs. 27.92 lakh crore in FY2021 from Rs. 14.39 lakh crore in FY2020, registering an annual growth of 94%. Transaction volumes remain strong in the current fiscal, with the markets clocking an ADTO of Rs. 56.36 lakh crore in H1 FY2022. The total market capitalisation for listed entities has also registered a strong growth. The market capitalisation of entities listed on the NSE increased to Rs. 258 lakh crore as of September 2021 from Rs. 203 lakh crore as of March 2021 and Rs. 112 lakh crore as of March 2020.
- **Surge in retail participation:** The increase in retail investors in capital markets can be witnessed in the new account openings in the industry. The total number of demat accounts increased to 674 lakh as of August 2021 and 551 lakh as of March 2021 from 408 lakh in March 2020 and 359 lakh in March 2019. This translates into a net addition of 12 lakh accounts per month in the last fiscal and 25 lakh accounts monthly addition this fiscal (April to August 2021), which is materially higher than the monthly addition of 4.08 lakh per month in FY2020. Anecdotal evidence suggests that equity markets have emerged as an unlikely beneficiary of the pandemic, with the work-from-home option, strong performance of stock markets, resurgence of initial public offerings (IPOs) and the use of technology for know your customer (KYC) attracting young investors and further facilitating the online account opening process. This, in turn, has supported online client acquisitions across different geographies.

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ABOUT ICRA

ICRA Limited (formerly Investment Information and Credit Rating Agency of India Limited) was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange.

Alliance with Moody's Investors Service

The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder. The participation of Moody's is supported by a Technical Services Agreement, which entails Moody's providing certain high-value technical services to ICRA. Specifically, the agreement is aimed at benefiting ICRA's in-house research capabilities, and providing it with access to Moody's global research base. The agreement also envisages Moody's conducting regular training and business seminars for ICRA analysts on various subjects to help them better understand and manage concepts and issues relating to the development of the capital markets in India. Besides this formal training programme, the agreement provides for Moody's advising ICRA on Rating-products strategy, and the Ratings business in general.

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- Provide information and guidance to institutional and individual investors/creditors;
- Enhance the ability of borrowers/issuers to access the money market and the capital market for tapping a larger volume of resources from a wider range of the investing public;
- Assist the regulators in promoting transparency in the financial markets;
- Provide intermediaries with a tool to improve efficiency in the funds raising process.

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