April 26, 2022

Sharekhan BNP Paribas Financial Services Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial Paper (IPO finance) Programme	3,000.00	3,000.00	[ICRA]A1+; reaffirmed
Commercial Paper Programme	1,000.00	1,000.00	[ICRA]A1+; reaffirmed
Total	**4,000.00**	**4,000.00**	

**Instrument details are provided in Annexure-1*

Rationale

While arriving at the rating, ICRA has taken a consolidated view of Sharekhan Limited (SKL) and its subsidiaries (hereon referred to as the SKL Group). The rating reaffirmation factors in SKL's strong parentage by virtue of being a part of the BNP Paribas Group (BNP Paribas SA (BNPP), rated Aa3/Stable/P-1 by Moody's, is SKL's ultimate parent) and its strategic importance to the parent. The rating also factors in SKL's considerable track record in the equity broking business, its well-established position in the retail broking space, and its healthy financial profile with adequate capitalisation and improved profitability.

While reaffirming the rating, ICRA has factored in SKL's high dependence on broking income, which remains susceptible to the extent of competition in the industry and the inherent volatility associated with capital markets. The Group's consolidated gearing increased in the last two fiscals, given the focus on growing the lending business {margin trade facility (MTF) book under SKL and capital market-based lending under Sharekhan BNP Paribas Financial Services Limited (SBPFSL)} coupled with the limited accrual to reserves due to the large dividend payout in FY2021. ICRA notes that the current capitalisation provides headroom to grow the funding business. However, if the hefty dividend payout ratio continues, the possibility of a further increase in the leverage cannot be ruled out. As on December 31, 2021, SKL's consolidated net worth was estimated at Rs. 1,500 crore and the consolidated gearing was estimated at 1.1 times compared to 0.5 times as on March 31, 2021 (0.1 times as on March 31, 2020). The rating also factors in the credit and market risks associated with the margin trading and capital market related lending businesses, given the nature of the underlying assets. Going forward, SKL's ability to scale up its lending business while maintaining adequate asset quality and capitalisation will remain a monitorable.

The rating also factors in SKL's foray into the discount broking segment, though the impact of discount broking on the consolidated financials remains nominal at present. The discount broking entity is expected to take a few years to scale up and break even. Going forward, SKL's ability to scale up the broking volume and maintain adequate profitability will also remain a key monitorable.

Key rating drivers and their description

Credit strengths

Strong parentage with strategic importance to parent – SKL is a wholly-owned subsidiary of BNPP. BNPP acquired a 100% stake in the company in FY2017 with the objective of entering the retail broking and allied lending business in India. BNPP has significant representation on SKL's board of directors; as on December 31, 2021, the company had a nine-member board with six representatives from BNPP, including two Whole-time Directors who ensure that SKL's operations are aligned with the parent's operations and policies. Moreover, certain management functions (such as risk and treasury) of SKL report directly to

BNPP. The ownership structure and co-branding[1], along with BNPP's regular supervision and control over the subsidiaries' activities, strengthen ICRA's assumption that SKL and SBPFSL will receive adequate support from the parent.

Long track record in capital markets related businesses and established position in retail broking – SKL has experience of over two decades in the equity broking space. It is a full-service stockbroking company, primarily engaged in the retail equity broking segment. In 9M FY2022, SKL reported an average daily turnover of Rs. 47,033 crore (Rs. 25,737 crore in FY2021) and its market share was 0.72% as on December 31, 2021. Apart from broking, SKL along with its subsidiary, SBPFSL, is engaged in various capital market related activities such as margin financing, loan against shares (LAS), initial public offering (IPO) financing, employee stock ownership plan (ESOP) financing, commodities trading, portfolio management services and mutual fund distribution. SKL is among the largest retail broking houses in the domestic broking landscape, with 24.7 lakh customers. It has a wide geographical presence with 3,597 franchisees and 136 branches as on December 31, 2021.

Healthy financial profile and adequate capitalisation – SKL and SBPFSL reported a healthy growth in revenues in 9M FY2022 and the consolidated profit after tax (PAT) is estimated to have correspondingly increased to Rs. 200 crore compared to Rs. 214 crore in FY2021 (Rs. 101 crore in FY2020). Despite the healthy PAT in FY2021, the accretion to reserves was impacted due to SKL's first-ever high dividend payout in December 2020. In the near term, SKL plans to continue making dividend payouts, though the quantum is expected to be lower compared to FY2021. As on December 31, 2021, SKL's consolidated capitalisation profile remained adequate with estimated net worth of Rs. 1,500 crore and gearing of 1.1 times. In the near term, incremental growth in the lending business will be debt-funded and the leverage is expected to increase further. However, the current capitalisation profile provides headroom for growing the lending business.

Credit challenges

High dependence on equity broking for revenue – The equity broking segment remains SKL's primary revenue driver, accounting for ~70% of the consolidated net operating income in FY2021 and 9M FY2022. Furthermore, SKL is predominantly a retail broking player with a negligible presence in the institutional broking and other capital market segments. The SKL Group started to focus actively on its lending business, which was primarily housed under SBPFSL, from FY2018 with plans of foraying into retail lending. SBPFSL subsequently realigned its strategy to focus on capital markets related lending products like margin funding, LAS, IPO finance and ESOP funding. The Group's lending business witnessed steady growth with the consolidated loan book increasing to ~Rs. 1,800 crore as on December 31, 2021 from Rs. 1,030 crore as on March 31, 2021 and Rs. 764 crore as on March 31, 2020.

Given the focus on MTF and other lending products, interest income is likely to grow over the medium term. However, with most of its revenues being linked to the inherently volatile capital markets, SKL's revenue profile and profitability remain vulnerable to market performance. Its ability to diversify its revenue stream, thus providing stability to its profitability, will remain a key rating monitorable.

Exposed to risks inherent in capital markets related businesses – SKL's earnings profile remains dependent on capital markets, which are inherently volatile in nature. Further, its MTF and LAS books pose asset quality risk in case of a sharp correction in the market. SKL remains exposed to credit and market risks, given the nature of the underlying assets, as any adverse event in the capital markets could erode the value of the underlying collateral stocks. However, the company's monitoring and risk management processes and the adequate performance of this business provide comfort.

Highly fragmented and competitive industry – The average yields for broking players have been under pressure, given the increasing competition in equity broking, the growing share of discount brokerage houses over the past couple of years and the significant surge in derivative volumes. Further, as SKL forays into the discount broking business, the flat brokerage model

[1] SKL's logo and signage include 'By BNP Paribas' while SBPFSL shares its name with the parent

is likely to exert pressure on the blended yields. The impact of the declining yields has been largely offset by the significant increase in the broking volumes and growing retail participation in the last two fiscals. Further, the current low level of equity market penetration indicates untapped potential for rapid expansion in the broking market. Going forward, the company's ability to grow its traditional as well as discount broking businesses, while maintaining adequate broking yields, will remain a key rating monitorable.

Liquidity position: Adequate

At the standalone level, SKL had an unencumbered cash balance of Rs. 664 crore and unutilised fund-based bank lines of Rs. 153 crore, as on February 28, 2022, to meet contingencies. It also had unutilised non-fund based bank facilities of Rs. 155 crore to meet any increase in the margin requirements at the exchanges. It had Rs. 1,340 crore of debt obligations (comprising commercial papers; CPs) outstanding as on February 28, 2022.

SBPFSL had an unencumbered cash balance of Rs. 43 crore as on February 28, 2022 while its total debt outstanding was Rs. 880 crore (comprising CPs).

SKL and SBPFSL have a demonstrated track record of raising funds through CPs. Further, the short-term and callable-on-demand nature of the MTF book of ~Rs. 900 crore (under SKL) and the LAS and MTF book of ~Rs. 925 crore (housed under SBPFSL) provides comfort. Thus, the overall liquidity at the consolidated level is adequate.

Rating sensitivities

Positive factors – Not applicable

Negative factors – A material change in SKL's shareholding or in its linkage with the parent could lead to a rating downgrade.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Rating Methodology for Entities in the Brokerage Industry Rating Methodology for Non-Banking Finance Companies Consolidation and Rating Approach Rating Approach - Implicit Support from Parent or Group
Parent/Group Support	Part of BNPP Group
Consolidation/Standalone	The rating is based on the consolidated financial statements of SKL

About the company

SBPFSL is a wholly-owned subsidiary of SKL and is registered with the Reserve Bank of India (RBI) as a non-banking financial company (NBFC). The company provides loans/finance to retail clients of the Group under various products such as LAS and funding for IPO, follow-on public offer (FPO), rights issue and ESOP/employee stock purchase scheme (ESPS). As on December 31, 2021, SBPFSL's loan book was Rs. 971 crore.

Sharekhan Limited

SKL is a security broking service provider registered with the Securities and Exchange Board of India (SEBI). Its main business activity is share broking, primarily in the retail segment, with a small presence in portfolio management services and the distribution of mutual fund products. SKL became a wholly-owned subsidiary of BNPP, a leading bank in Europe, in FY2017.

SKL, which is a member of the Bombay Stock Exchange (BSE), the National Stock Exchange (NSE), the Metropolitan Stock Exchange of India Limited (MSEI) and the Multi Commodity Exchange (MCX), is also a depository participant with National Securities Depository Limited (NSDL) and Central Depository Services Limited (CDSL). As on December 31, 2021, SKL's client base was 24.7 lakh and the broking volumes were largely contributed by the franchises. As on December 31, 2021, the company had 3,597 franchisees and 136 branches.

Key financial indicators (audited)

SKL Consolidated	FY2019	FY2020	FY2021
Brokerage Income (Rs. crore)	466.9	488.2	733.4
Fee Income (other than broking; Rs. crore)	78.10	85.30	86.5
Net Interest Income (Rs. crore)	182.6	199.9	209.0
Other Non-interest Income (Rs. crore)	49.00	21.40	15.1
Net Operating Income (NOI; Rs. crore)	776.6	794.9	1,044.0
Total Operating Expenses (Rs. crore)	708.9	641.0	751.9
Profit before Tax (Rs. crore)	67.0	140.1	288.4
Profit after Tax (PAT; Rs. crore)	33.8	100.6	214.4
Net Worth (Rs. crore)	1,673.2	1,768.0	1,382.6
Borrowings (Rs. crore)	0.0	97.8	633.0
Gearing (times)	0.0	0.1	0.5
Cost-to-Income Ratio (%)	91.1%	80.3%	72.0%
Return on Net Worth (%)	2.3%	5.8%	13.6%
PAT/NOI (%)	4.3%	12.6%	20.5%

Source: *Company, ICRA Research; All ratios as per ICRA calculations*

SBPFSL Standalone	FY2019	FY2020	FY2021	9M FY2022*
Total Income (Rs. crore)	82.1	94.7	103.3	115.8
Profit after Tax (Rs. crore)	(20.9)	41.1	45.7	53.6
Net Worth (Rs. crore)	472.1	513.1	488.5	542.0
Loan Book (net; Rs. crore)	755.9	673.5	638.4	966.60
Total Assets (Rs. crore)	791.8	700.0	733.6	1,129.5
Return on Assets (%)	-2.8%	5.5%	6.4%	7.6%
Return on Net Worth (%)	-4.3%	8.3%	9.1%	13.9%
Gross Gearing (times)	0.6	0.4	0.5	1.1
Gross NPA (%)	0.0%	0.1%	0.0%	0.0%
Net NPA (%)	0.0%	0.1%	0.0%	0.0%
CRAR (%)	44.7%	63.8%	66.4%	49.3%

Source: *Company, ICRA Research; *Provisional ad unaudited; All ratios as per ICRA calculations*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Type	Current Rating (FY2023)			Chronology of Rating History for the Past 3 Years										
			Amount Rated (Rs. crore)	Amount Outstanding as of Mar 31, 2022 (Rs. crore)	Date & Rating in FY2023	Date & Rating in FY2022		Date & Rating in FY2021		Date & Rating in FY2020						
					Apr 26, 2022	Jun 18, 2021	May 20, 2021	Sep 10, 2020	Jul 31, 2020	Mar 05, 2020	Oct 09, 2019	Sep 20, 2019	Aug 01, 2019	Jul 03, 2019	May 17, 2019	Apr 16, 2019
1	CP Programme	Short Term	1,000.0	680.0	**[ICRA]A1+**	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+
2	CP (IPO finance) Programme	Short Term	3,000.0	0.0	**[ICRA]A1+**	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	-	-	-	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
CP Programme	Very Simple
CP (IPO finance) Programme	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE550X14839	CP Programme	Jan 17, 2022	4.37%	Apr 18, 2022	100.0	[ICRA]A1+
INE550X14847	CP Programme	Jan 21, 2022	4.25%	Apr 22, 2022	115.0	[ICRA]A1+
INE550X14862	CP Programme	Feb 4, 2022	4.75%	May 6, 2022	365.0	[ICRA]A1+
INE550X14870	CP Programme	Mar 9, 2022	4.60%	Jun 8, 2022	100.0	[ICRA]A1+
NA	CP Programme (yet to be placed)	-	-	7-365 days	320.00	[ICRA]A1+
NA	CP (IPO finance) Programme (yet to be placed)	-	-	7-30 days	3,000.00	[ICRA]A1+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Company Name	SKL Ownership	Consolidation Approach
Sharekhan Limited	Holding Company	Full Consolidation
Sharekhan BNP Paribas Financial Services Limited	100% (Rated Entity)	Full Consolidation
Sharekhan Commodities Private Limited	100%	Full Consolidation
Wealthtiger Investment Advisors Private Limited	100%	Full Consolidation
Sharekhan Consultants Private Limited	100%	Full Consolidation
Sharekhan.com India Private Limited	100%	Full Consolidation
Espresso Financial Services Private Limited	100%	Full consolidation

Source: *Company; As on December 31, 2021*

Note: *ICRA has taken a consolidated view of the parent (SKL) and its subsidiaries while assigning the rating*

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