

March 26, 2024

Cholamandalam Securities Limited: [ICRA]A1+ assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Commercial paper	250.00	[ICRA]A1+; assigned
Total	250.00	

*Instrument details are provided in Annexure I

Rationale

The rating factors in Cholamandalam Securities Limited's (CSEC's) strong parentage; it is a wholly-owned subsidiary of Cholamandalam Investment and Finance Company Limited (CIFCL; rated [ICRA]AA+ (Positive)/[ICRA]AA (Positive)/[ICRA]A1+). CSEC derives operational, managerial and financial support from CIFCL and both entities share a common brand name. Operationally, CSEC is able to leverage CIFCL and Murugappa Group's diverse presence and businesses for augmenting its franchise and reach. ICRA also notes that CIFCL and Cholamandalam Home Finance Limited (CHFL) have extended short-term credit facilities to CSEC, supporting its funding requirements to a significant extent at present. Going forward as well, ICRA expects timely capital, liquidity and other support from CIFCL and Murugappa Group, if required.

The rating takes note of CSEC's modest scale and the correspondingly limited business diversification at present. The rating also factors in the risk arising from the inherent volatility in the company's operations, given the linkages with capital markets. The intense competition in the broking industry can have a bearing on CSEC's volumes in the broking segment, especially during market downcycles. Going forward, the company is expected to scale up its margin trading facility (MTF) book, which would lead to an increase in the leverage from the current level. CSEC's financial profile is currently moderate and it would require timely support from the parent for meeting its growth plans while keeping its leverage under control.

Key rating drivers and their description

Credit strengths

Strong parentage; wholly-owned subsidiary of CIFCL – As CSEC is a 100% subsidiary of CIFCL, it is expected to derive operational, managerial and financial support from the parent. CSEC's board has four directors, including two directors from CIFCL. Operationally, CSEC derives synergies by tapping the captive customer and vendor bases of Murugappa Group. The Group's franchise and reach, coupled with its established presence across various businesses and franchises, augurs well for CSEC to execute its business plan. CIFCL and CHFL have extended short-term credit facilities to CSEC with the outstanding amount at Rs. 123 crore (sanctioned amount was Rs. 220 crore) as of December 2023. ICRA expects timely capital, liquidity and operational support from CIFCL and Murugappa Group, if required.

Credit challenges

Modest scale and limited diversification at present – CSEC primarily offers broking services to retail and institutional clients; it operates at a modest scale at present, with 24,187 active retail and 27 institutional clients. Apart from broking, it acts as a distributor of financial products. The scale-up of CSEC's operations would be modest in the near-to-medium term due to the competitive landscape and would depend on its ability to augment its client base. Its income profile is currently concentrated towards broking income and distribution income, which accounted for ~40-50% each of the net operating income (NOI) on

average during FY2019-FY2023. The share of distribution income increased to 74% in 9M FY2024 because of an insurance contract sourced through CIFCL. The company also commenced its MTF business, with this segment accounting for around 6% of its income. As a result, the share of broking income declined to around 20% in 9M FY2024.

As CIFCL has obtained a corporate insurance agent licence, CSEC will no longer do group-related insurance contracts. On the other hand, given CSEC's focus on increasing its MTF book (Rs. 127.2 crore as of December 2023 and Rs. 76.7 crore as of March 2023), the revenue mix is expected to become more diversified with 50:30:20 from broking income, MTF income and other income, going forward.

Moderate financial risk profile; timely capital infusion required for meeting growth plans – CSEC has a moderate earnings profile, with its modest scale constraining its operational efficiency. It recorded a profit after tax (PAT) of Rs. 6.4 crore in FY2023 (PAT/NOI of 12.9% and PAT/Net worth of 12.3%) compared to Rs. 5.4 crore in FY2022 (PAT/NOI of 13.5% and PAT/Net worth of 12.3%). The company's PAT improved in 9M FY2024 on the back of one-time income from insurance distribution (Rs. 51.4 crore) and gain on the sale of investments (Rs. 22.7 crore). However, adjusting for these items, the profit remained modest. The company is currently scaling up its employee base and investing in operating infrastructure to support the envisaged growth over the near-to-medium term. ICRA expects economies of scale to kick in, going forward, as the company augments its client profile and increases its MTF book, which would support an improvement in its earnings profile.

CSEC's net worth stood at Rs. 56.5 crore as of December 2023 (Rs. 50.7 crore as of March 2023). Despite healthy internal generation of Rs. 57.9 crore in 9M FY2024, the net worth increased slightly, given the sizeable dividend payment of Rs. 52.1 crore to the parent. An additional Rs. 15 crore of dividend is expected to be declared in Q4 FY2024, which could impact the net worth as of March 2024. Coupled with the expected growth in the MTF book, the gearing is expected to increase from 2.2 times as of December 2023. The company avails borrowings largely for its MTF book, which shall be a key focus segment going forward. This shall impact the capitalisation profile unless adequate capital is infused. CSEC envisages maintaining a gearing of 3.0-3.5 times, going forward. CIFCL is expected to infuse capital, if required, to keep CSEC's leverage under control.

Dependence on capital markets, which are inherently volatile and cyclical in nature – CSEC's revenues and profits remain dependent on capital markets, which are inherently volatile in nature. Moreover, with increasing competition in equity broking and the advent of discount brokerage houses, the average yields for broking players have been under pressure. With the competitive intensity in the industry expected to remain high, the pressure on the industry margin is expected to continue.

Liquidity position: Adequate

In order to maintain margin at the exchanges, CSEC utilises its sanctioned non-fund based bank lines, aggregating Rs. 48 crore (backed by lien marked fixed deposits of Rs. 24 crore), besides cash & cash equivalents, securities, and client funds. The utilisation of cash margins placed with the exchanges averaged about 15% during the 12-month period ending February 2024. As of December 31, 2023, CSEC had a current account balance of Rs. 1.5 crore and liquid investments of Rs. 8 crore. Additionally, short-term loans from Group entities, for extending MTF to clients, stood at Rs. 123 crore as of December 2023.

Rating sensitivities

Positive factors – Not applicable

Negative factors – A material change in the expected level of support from CIFCL or a material deterioration in the credit risk profile of CIFCL shall impact CSEC's rating.

Analytical approach

Analytical approach	Comments
Applicable rating methodologies	Rating Methodology – Stockbroking & Allied Services
Parent/Group support	The rating factors in CSEC's strong parentage as it is a subsidiary of CIFCL. CSEC draws managerial, operational and financial support from CIFCL, as evident from the common board member, credit lines and shared brand name.
Consolidation/Standalone	Standalone

About the company

Incorporated in 1994, Cholamandalam Securities Limited (CSEC) is a wholly-owned subsidiary of CIFCL and a part of Murugappa Group. CSEC is a Securities and Exchange Board of India (SEBI) registered stockbroker and depository participant. The company is a member of BSE Limited and National Stock Exchange of India Limited. It is also a depository participant with National Securities Depository Limited (NSDL) and Central Depository Services (India) Limited. The company offers stockbroking and depository services to retail clients and institutional investors, including mutual funds, insurance companies, etc.

CSEC had 24,187 retail clients and 27 institutional clients through a network of 20 branches and 50 franchises as of December 2023. The company reported a net profit of Rs. 6.4 crore on net operating income of Rs. 43.0 crore in FY2023 vis-à-vis a net profit of Rs. 5.4 crore on net operating income of Rs. 34.5 crore in FY2022.

Key financial indicators (audited)

CSEC – Standalone	FY2022	FY2023	9M FY2024*
Net operating income	34.5	43.0	96.2
Profit after tax	5.4	6.4	64.6
Net worth	53.1	50.7	56.5
Total assets	105.4	169.6	329.8
Gearing (times)	0.1	1.2	2.2
Return on average net worth	12.3%	12.3%	160.6%

Source: Company, ICRA Research; Amount in Rs. crore; *Provisional

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Current rating (FY2024)		Chronology of rating history for the past 3 years			
		Amount rated (Rs. crore)	Amount outstanding as of Mar 26, 2024 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
				Mar 26, 2024	-	-	-
1 Commercial paper	Short term	250.0	-	[ICRA]A1+			

Complexity level of the rated instruments

Instrument	Complexity Indicator
Commercial paper	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: [Click Here](#)

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
Yet to be placed	Commercial paper	NA	NA	NA	250.0	[ICRA]A1+

Source: Company

Annexure II: List of entities considered for consolidated analysis – Not applicable

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Branches



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