

July 31, 2020

## Sharekhan Limited: Rating reaffirmed

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial paper programme	500.00	500.00	[ICRA]A1+; reaffirmed
<b>Total</b>	<b>500.00</b>	<b>500.00</b>	

\*Instrument details are provided in Annexure-1

### Rationale

The reaffirmation of the rating for the commercial paper (CP) programme of Sharekhan Limited (SKL) factors in its strong parentage by virtue of being a part of the BNP Paribas Group (BNP Paribas S.A. (BNPP); rated Aa3/Stable/P-1 by Moody's), the company's considerable track record in the equity broking business and its well-established position in the retail broking space with a widespread clientele. The rating also factors in SKL's healthy capital structure (gearing of 0.06 times as on March 31, 2020) and comfortable liquidity profile, on a consolidated basis, with sizeable cash and liquid investments and unutilised bank lines as on March 31, 2020.

The rating continues to factor 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. While reaffirming the rating, ICRA has taken note of SKL's decision to foray into the discount broking business under a new subsidiary with a new brand name. The new venture is expected to commence operations in H2 FY2021 and would entail an investment of ~Rs. 100 crore spread over FY2021-FY2022. The company reported a healthy profitability level at a consolidated basis in FY2020 (profit after tax/net operating income (PAT/NOI) of 12.66%) after a subdued performance (PAT/NOI of 4.35%) in the previous fiscal owing to the one-time write-offs associated with the lending business. Going forward, given its foray into discount broking and the competitive pressure, the company's ability to maintain healthy profitability while scaling up its operations and diversifying its revenue stream would remain critical from a credit perspective.

### Key rating drivers and their description

#### Credit strengths

**Strong parentage with strategic importance to parent** – SKL is a wholly-owned subsidiary of the BNPP Group. 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. Moreover, certain management functions (such as risk and treasury) of SKL report directly to BNPP. The ownership structure and the shared brand name, along with BNPP's regular supervision and control over the subsidiaries' activities, strengthen ICRA's assumption that SKL and Sharekhan BNP Paribas Financial Services Limited (SBPFSL), a wholly-owned subsidiary of SKL, will receive timely and adequate financial and operational 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 with a marginal presence in the institutional broking segment. Apart from broking, SKL is

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engaged in various capital market related activities such as margin financing, commodities trading, portfolio management services and mutual fund distribution. SKL is among the largest retail broking houses in the domestic broking landscape, with ~20 lakh customers. It has a wide geographical presence with 3,502 franchisees and 142 branches as on March 31, 2020.

**Comfortable liquidity position and capitalisation** – SKL has a comfortable capital structure with a consolidated gearing of 0.06 times as on March 31, 2020. It reported a healthy consolidated net worth of Rs. 1,768.00 crore as on March 31, 2020. SKL had a loan book of Rs. 766 crore (consolidated; primarily held in SBPFSL) as on March 31, 2020. The lending operations have been funded through own funds, though the company has occasionally borrowed through the issuance of commercial papers. Going forward, SKL is expected to make regular dividend payouts, which will impact its internal accruals. The company announced a dividend payout of Rs. 34 per share (face value of Rs. 10), which aggregates to an outgo of Rs. 199.70 crore (subject to shareholders' approval). The dividend outgo announced for FY2020 is ~2 times the PAT for the year. With regular dividend payouts planned by the company and given its focus on growing the loan book, the dependence on external borrowings is expected to increase though the overall gearing would remain in a comfortable range.

## Credit challenges

**High dependence on equity broking for revenue** – The equity broking segment remains SKL's primary revenue driver, accounting for ~63% of the NOI in FY2020. Furthermore, SKL is predominantly a retail broking player with a negligible presence in the institutional broking and other capital market segments. Further, as it forays into the discount broking business, the flat brokerage model is likely to exert pressure on the blended yields. Going forward, the company's ability to diversify its revenue stream and grow its traditional and discount broking businesses while maintaining the margins will remain a key rating monitorable.

**Highly fragmented and competitive industry** – With increasing competition in equity broking and the advent of discount brokerage houses over the past few years, the average yields for broking players have been under pressure. However, the low level of equity market penetration indicates huge untapped potential for rapid expansion in the broking market. Also, with most of its revenues being linked to the inherently volatile capital markets, SKL's revenue profile and profitability remain vulnerable to market performance. Given its foray into discount broking and the competitive pressure, the company's ability to scale up this business profitably would remain critical over the medium term.

## Liquidity position: Strong

SKL needs funds to place margins at the exchange and for its lending business. It also takes margin deposits from its clients, which are placed at the exchanges, and has ready access to the clients' assets, which can be monetised without a significant lag. At the consolidated level, SKL had an unencumbered cash and bank balance of Rs. 766 crore, liquid investments of Rs. 165 crore and sufficient unutilised bank lines as on March 31, 2020. It had a loan book of Rs. 766 crore as on March 31, 2020 and a significant portion of the lending operations are funded through own funds (borrowings of only Rs. 97.80 crore). As on May 31, 2020, SKL (standalone) had unencumbered cash and liquid investments of Rs. 333 crore and SBPFSL had a cash balance of Rs. 156 crore. With the liquidity being sufficient to cover the near-term debt obligations (Rs. 97.80 crore maturing in August 2020), the company's liquidity position is strong.

## Rating sensitivities

**Positive triggers** – Not applicable

**Negative triggers** – A material change in SKL's shareholding or its linkage with the parent coupled with a significant deterioration in its business and financial performance could result in a rating downgrade.

## Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">ICRA's Credit Rating Methodology for Brokerage Houses</a> <a href="#">ICRA's Credit Rating Methodology for Non-Banking Finance Companies</a> <a href="#">Financial consolidation and rating approach</a>
Parent/Group Support	Part of BNPP Group
Consolidation/Standalone	The rating is based on the consolidated financial statements of SKL

## About the company

Incorporated in 2007, SKL is a security broking service provider registered with the Securities and Exchange Board of India (SEBI). The company's 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 BNP Paribas S.A., 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).

## Key financial indicators

### Sharekhan Limited (consolidated)

Rs. crore	FY2018 Ind-AS	FY2019 Ind-AS	FY2020 Ind-AS
Brokerage Income (net)	500.9	466.9	488.2
Fee Income (other than broking)	25.0	31.9	42.3
Net Interest Income	156.8	182.6	199.9
Other Non-interest Income	106.4	74.8	41.9
Net Operating Income	808.1	776.6	794.9
Total Operating Expenses	654.8	708.9	641.0
Profit before Tax	152.3	67.0	140.1
Profit after Tax	99.0	33.8	100.6
Loans and Advances	750.30	862.10	766.00
Net Worth	1,305.7	1,673.2	1,768.0
Gearing (times)	0.26	0.00	0.06
Return on Net Worth	7.88%	2.27%	5.85%

Source: Company & ICRA research

**Sharekhan Limited (standalone)**

Rs. crore	FY2018	FY2019	FY2020
	Ind-AS	Ind-AS	Ind-AS
Brokerage Income (net)	500.9	466.9	488.2
Fee Income (other than broking)	1.0	0.6	1.2
Net Interest Income	123.3	130.7	140.2
Other Non-interest Income	98.3	83.7	57.8
Net Operating Income	723.5	681.9	687.4
Total Operating Expenses	613.3	601.2	604.2
Profit before Tax	107.3	79.5	80.2
Profit after Tax	67.6	49.2	51.5
Net Worth	1,122.6	1,505.6	1,551.7
Gearing (times)	0.3	0.0	0.0
Return on Net Worth	6.20%	3.74%	3.37%

Source: Company & ICRA research

**Status of non-cooperation with previous CRA: Not applicable**
**Any other information: None**
**Rating history for last three years**

	Instrument	Current Rating (FY2021)				Chronology of Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding*	31-Jul-20	FY2020	FY2019	FY2018
						03-Jul-19	31-May-18	28-Apr-17
1	Commercial Paper	Short Term	500.00	0.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

\* Outstanding as on March 31, 2020; Amount in Rs. crore

**Complexity level of the rated instrument**

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website [www.icra.in](http://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
NA	Commercial Paper	NA	NA	7-365 days	500.00	[ICRA]A1+

Source: Company

### Annexure-2: List of entities considered for consolidated analysis

The subsidiaries considered in the consolidated financial statements as of March 31, 2020:

Company Name	Ownership	Consolidation Approach
<b>Subsidiaries</b>		
Sharekhan BNP Paribas Financial Services Limited	100.00%	Full Consolidation
Sharekhan Commodities Private Limited	100.00%	Full Consolidation
Sharekhan.com India Private Limited	100.00%	Full Consolidation
Sharekhan Consultants Private Limited	100.00%	Full Consolidation
Wealthtiger Investment Advisors Private Limited	100.00%	Full Consolidation

Source: Company

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## About ICRA Limited:

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