May 05, 2021

Emkay Global Financial Services Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Short-term Non-fund Based Bank Facilities	275.00	275.00	[ICRA]A2+; reaffirmed
Total	**275.00**	**275.00**	

**Instrument details are provided in Annexure-1*

Rationale

While reaffirming the rating, ICRA has taken a consolidated view of the business and financial profiles of Emkay Global Financial Services Limited (EGFSL) and its five subsidiaries, together referred to as the Group or EGFSL.

The rating factors in the Group's demonstrated track record of over 25 years in the financial services industry, its comfortable capitalisation profile and its established presence in the institutional broking segment with a strong clientele. The rating is, however, constrained by the limited diversification in the Group's revenue profile, the inherent volatility in the capital markets and the highly competitive and fragmented nature of the broking industry. The compression in yields over the past few years, owing to changes in the product mix and competitive pressure across the industry, along with high operating expenses and weaker-than-expected performance of the wealth management business had resulted in subdued profitability in FY2020. ICRA, however, has noted the improvement in EGFSL's consolidated profitability in 9M FY2021, albeit supported by mark-to-market (MTM) gains on investments. Going forward, EGFSL's ability to diversify its earnings profile, achieve a significant and sustained improvement in the profitability of its core operations and maintain a healthy capitalisation profile remains critical from a credit perspective.

Key rating drivers and their description

Credit strengths

Long track record in capital market related business – The Group has a track record of over 25 years in capital markets with a presence in equity, currency and commodity broking along with lending, investment banking, alternative assets and wealth management services for its clients. It caters to ~1.45 lakh customers through its network of 18 branches and 150+ franchises spread across ~79 cities.

Established presence in broking business – EGFSL has an established presence in the equity broking business with a focus on the institutional & high net worth individuals (HNI) segment. As of December 31, 2020, EGFSL had a strong presence in the institutional broking business with more than 300 clients comprising a mix of domestic institutional investors and foreign portfolio investors. On the back of the traction in its institutional segment, EGFSL witnessed a healthy growth in its broking turnover to Rs. 164.5 lakh crore accounting for a 3.9% market share of the overall industry turnover in 9M FY2021 compared to Rs. 37.0 lakh crore and a 1.0% market share in FY2020.

Since FY2020, the company has focused on leveraging its infrastructure for catering to institutional customers oriented towards direct market access (DMA) arrangements. Additionally, it implemented a bespoke low latency solution for a high frequency trading (HFT) client in FY2020. With significant broking contribution (~95% of the institutional turnover) from the HFT client in 9M FY2021, EGFSL registered a robust growth in its institutional broking turnover to Rs. 158.8 lakh crore, accounting for ~7% of the industry institutional market share. Further, led by the healthy traction in the futures and options (F&O) segment, the retail broking turnover witnessed a sizeable material growth to Rs. 5.7 lakh crore in 9M FY2021 from Rs. 2.2 lakh crore in FY2020.

Adequate capitalisation level for current scale of operations – The Group is well capitalised for the current scale of operations with a net worth of Rs. 159.5 crore as on December 31, 2020. Its fund-based borrowing requirements are primarily used for scaling the loan against the share book of the non-banking financial company's (NBFC) arm. In addition to fund-based borrowings, it avails bank guarantees for meeting the margin requirements of the broking operations at the exchange houses. With a decline in the loan book in 9M FY2021, the fund-based borrowings declined to ~Rs. 1 crore as on December 31, 2020, leading to an improvement in the gearing to 0.01 times from 0.05 times as of March 31, 2020.

Credit challenges

Subdued profitability in FY2020 though improvement witnessed in 9M FY2021 on account of net fair value gain – The Group's profitability indicators moderated in FY2020 primarily due to the diminution of its investment book, elevated operating expenses and the slower-than-expected ramp-up of its wealth management business, with the Group reporting a net loss of Rs. 11.9 crore (PY: profit after tax (PAT) of Rs. 8.4 crore). However, the Group reported an improvement in its profitability in 9M FY2021 on a consolidated basis, which was primarily supported by net fair value gains of Rs. 14.4 crore (Rs. 11.8 crore remained unrealised as of December 31, 2020). Nevertheless, it continued to witness elevated cost-to-income levels in its core operations at 108.4%. Going forward, the Group's ability to improve the profitability of its core operations on a sustained basis remains critical from a credit perspective.

Exposed to risks inherent in capital market related businesses – The Group's operations are linked to the inherently volatile capital markets. Thus, its revenue profile and profitability remain vulnerable to market performance. ICRA notes that any downturn in the capital markets may directly impact the fair value of the Group's investment book as witnessed in Q4 FY2020, thereby putting pressure on the overall profitability. Further, the Group's revenue profile remains concentrated with broking income accounting for ~81% of the operating income in 9M FY2021 and is yet to witness meaningful diversification through the scale-up of business in the wealth management segment. Nonetheless, the Group's efforts towards stabilising the revenue profile through flat fee arrangements among new institutional clients provide some comfort.

Intense competition in capital markets – With increasing competition in equity broking, the advent of discount brokerage houses and a significant surge in derivative volumes, the average yields for broking players have been under pressure. EGFSL's traditional trading segments (excluding broking through DMA and HFT arrangements) witnessed a decline in the blended yields to 0.67 bps in 9M FY2021 from 1.09 bps in FY2020. Going forward, with increasing competition, the industry margin is expected to remain under pressure.

Liquidity position: Adequate

The Group's liquidity requirement is primarily for placing margins at the exchanges and growing the loan against shares (LAS) book. The company deployed an average of ~Rs. 315 crore of margins at the exchanges (funded through own and client funds/securities) during September 2020 and February 2021, with margin utilisation ranging between 47% and 61% during this period. Additionally, the Group avails intraday loans of ~Rs. 185 crore, which support the working capital requirements of the broking operations. The Group had non-fund based sanctioned limits of Rs. 221 crore secured against 50% of bank deposits; the average utilisation based on sanctioned limits in these facilities varied between 57% and 75% during April 2020 to January 2021. As on January 31, 2021, the Group had nil fund-based borrowings and the utilisation of non-fund based limits stood at Rs. 165 crore (against a drawing power of Rs. 167 crore). Further, it had an unencumbered cash and bank balance of ~Rs. 43 crore and unutilised but drawable fund-based limits of Rs. 40 crore as of January 31, 2021, which are sufficient to cover any short-term debt obligations in case the need arises.

Rating sensitivities

Positive factors – ICRA could upgrade the rating if there is a significant and sustained improvement in the profitability with a meaningful diversification in the revenue stream while maintaining a comfortable capitalisation profile.

Negative factors – The rating could be revised if the Group reports losses leading to a significant deterioration in its net worth or a deterioration in the asset quality of the lending business or liquidity position. Pressure on the rating could also arise if there is any change in the regulatory environment, which may adversely impact the company's business operations and financial performance.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Rating Methodology for Entities in the Brokerage Industry Consolidation and Rating Approach
Parent/Group Support	Not Applicable
Consolidation/Standalone	To arrive at the rating, ICRA has considered the consolidated financial profile of EGFSL, along with its subsidiaries. Details of these companies are provided in Annexure-2

About the company

EGFSL was founded in January 1995 as Emkay Share and Stock Brokers Private Limited by two first-generation entrepreneurs. The constitution of the company was changed to public limited in October 2005 and it was renamed Emkay Share and Stock Brokers Limited. In July 2008, the name was changed to Emkay Global Financial Services Limited. Currently, the company, along with its wholly-owned subsidiaries, is engaged in various activities such as equity broking, commodity broking, currency broking, lending, depository participant, wealth/portfolio management services, distribution of financial products and investment banking operations.

On a consolidated basis, EGFSL reported a net loss of Rs. 11.9 crore on net operating income (NOI) of Rs. 110.3 crore in FY2020 compared to a net profit of Rs. 8.4 crore on NOI of Rs. 123.3 crore in FY2019. In 9M FY2021, EGFSL reported a net profit of Rs. 5.7 crore on NOI of Rs. 83.9 crore.

Key financial indicators

EGFSL (Consolidated)	FY2019	FY2020	9M FY2021*
Net Brokerage Income	94.1	87.9	68.0
Net Interest Income	9.3	6.8	4.2
Other Non-interest Income	20.0	15.6	11.8
Net Operating Income	123.3	110.3	83.9
Total Operating Expenses	109.2	120.4	91.0
Profit before Tax	12.2	-16.8	8.5
Profit after Tax	8.4	-11.9	5.7
PAT/NOI	6.8%	-10.8%	6.7%
Cost-income Ratio	88.5%	109.1%	108.4%
Net Worth	167.1	152.8	159.5
Gearing (times)	0.13	0.05	0.01
Return on Net Worth	5.1%	-7.4%	4.8%

Source: *Company, ICRA research; *Provisional figures; All ratios as per ICRA calculations; Amount in Rs. crore*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)				Chronology of Rating History for the Past 3 Years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Current Rating	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019
					May 05, 2021	Apr 30, 2020 Apr 03, 2020	Mar 20, 2019	Feb 28,2018
1	Non-fund Based Bank Guarantee	Short Term	275.00	161.00*	**[ICRA]A2+**	**[ICRA]A2+**	**[ICRA]A1**	**[ICRA]A1**

Source: *Company, *As of March 17, 2021*

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 click here

Annexure-1: Instrument details

ISIN No.	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Non-fund Based Bank Guarantee	NA	NA	NA	221.00	[ICRA]A2+
NA	Unallocated	NA	NA	NA	54.00	[ICRA]A2+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Emkay Fincap Limited	100% Subsidiary	Full Consolidation
Emkay Investment Managers Limited	100% Subsidiary	Full Consolidation
Emkay Wealth Advisory Limited (Formerly Emkay Insurance Brokers Limited)	100% Subsidiary	Full Consolidation
Emkay Commotrade Limited	100% Subsidiary	Full Consolidation
EmkayGlobal Financial Services IFSC Private Limited	100% Subsidiary	Full Consolidation

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About ICRA Limited:

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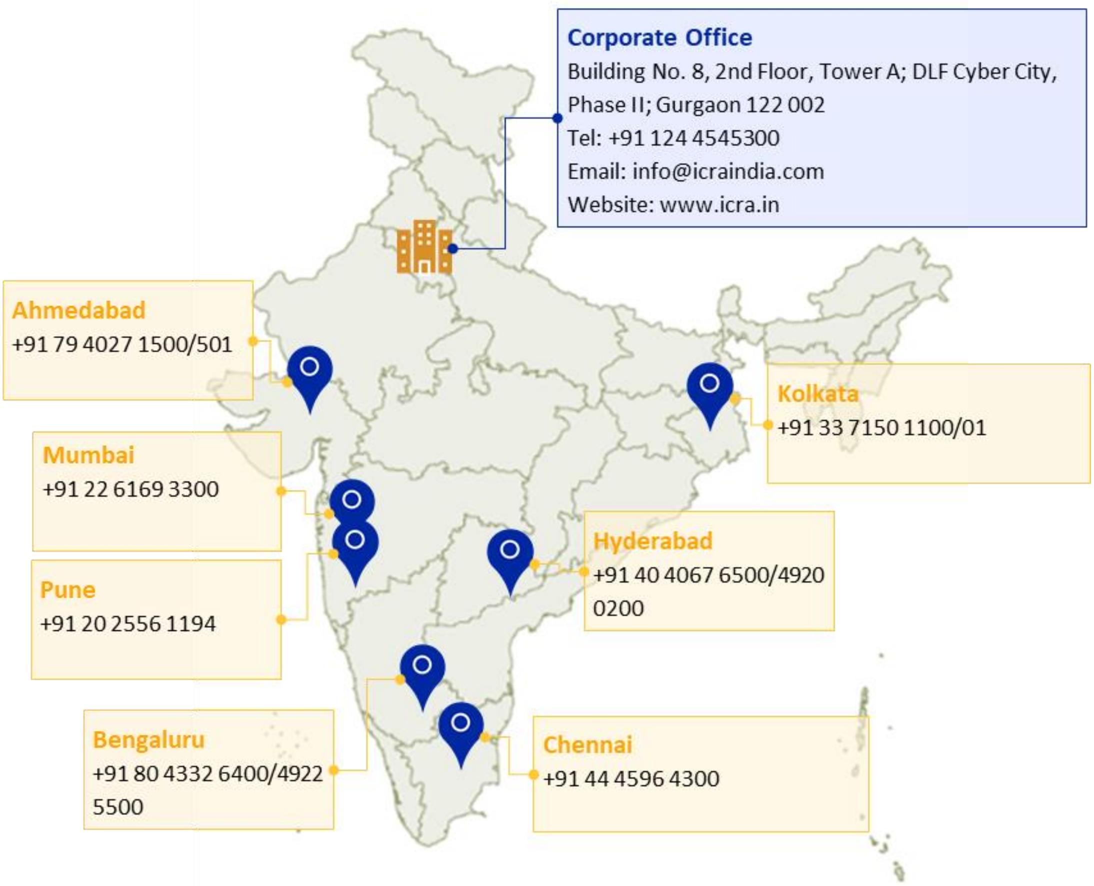

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