

ICICI Securities

Estimate change



TP change



Rating change



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Bloomberg	ISEC IN
Equity Shares (m)	322
M.Cap.(INRb)/(USD\$)	170.6 / 2.3
52-Week Range (INR)	569 / 191
1, 6, 12 Rel. Per (%)	5/31/136
12M Avg Val (INR M)	#N/A

Financials & Valuations (INR b)

Y/E March	2020	2021E	2022E
Revenues	17.3	22.6	23.5
Opex	9.7	12.2	12.1
PBT	7.5	10.4	11.4
PAT	5.4	7.7	8.5

Ratios

C/I ratio (%)	56.3	53.9	51.5
PAT margin (%)	31.4	34.3	36.3
RoE (%)	48.1	58.4	54.3
Div. Payout (%)	68.9	70.0	70.0
EPS	16.8	24.0	26.4

Valuations

P/E (x)	31.5	22.0	20.0
P/BV (x)	14.1	11.8	10.1
Div. Yield (%)	2.1	3.2	3.5

Shareholding pattern (%)

As On	Jun-20	Mar-20	Jun-19
Promoter	79.2	79.2	79.2
DII	10.2	11.5	12.4
FII	3.8	3.2	1.6
Others	6.8	6.2	6.8

FII Includes depository receipts

CMP: INR530
TP: INR625 (+18%)
Buy

Strong performance in equity brokerage; Upgrade est. by ~15%

- ICICI Securities (ISEC) delivered 47% YoY growth in PBT to INR2.6b (15% beat). However, lower tax rate YoY (25.6% vs 35.4% a year ago) led to PAT growth of 70% to INR1.9b.
- The quarter was characterized by strong growth in the brokerage business (+24% QoQ and +62% YoY), partly offset by muted performance in distribution (-20% QoQ and -30% YoY). Investment banking revenues were healthy at INR220m (+34% YoY and more than doubled QoQ). **C/I ratio was down 370bp YoY to 52.5% driven largely by operating leverage.**
- **On back of continued momentum in equity brokerage business and healthy pipeline in investment banking business, we have upgraded earnings by ~17/13% for FY21/22. Buy with target price of INR625 (24x FY22 EPS).**

Gaining market share in cash and derivatives trading

- In a quarter marked by heightened trading (industry cash equity ADTO was up 60%+ YoY), ISEC gained market share from peers. **Market share improved 260bp/150bp YoY in the cash/derivatives segments to 10.7%/8.9%.** Thus, equity ADTO more than doubled to ~INR50b. ADTO in the derivatives segment grew 32% YoY to INR817b (vs 9% for the industry).
- The 'Prime' platform continues to gain traction – **ISEC on-boarded 65k customers, taking the total to 375k (i.e. 35% of NSE active customers).**

Distribution income remains muted

- Distribution income declined ~20% to INR800m driven by 12% YoY decline in MF distribution revenue and 25% YoY decline in other income. **In the case of MF and LI distribution, both, this quarter's revenue was the lowest in more than the past 12 quarters.**
- Investment banking revenue was INR220m (+35% YoY). ISEC has 13 companies in deal pipeline amounting to INR382b. With the healthy deal pipeline we estimate 30% YoY growth in FY21.

Key concall highlights

- Quarterly customer acquisition slowed down from 110k to 80k QoQ as the end-to-end digital account opening option in was ready only by end-April.
- **ICICIB contributed 65% of incremental customers acquired vs 80% QoQ.**

Other highlights

- Given the surge in trading volumes, the lending book too jumped from INR6b to INR15b QoQ. Although average Quarterly lending book declined QoQ. NII from this division stood at INR230m vs INR175m a year ago and INR335m a quarter ago.
- Employee expenses jumped 24% QoQ due to variable component payments on account of strong company performance.
- Total employee count down 13% YoY and 2% QoQ to 3,729

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Valuation and view

Over the past year, initiatives such as the ICICI Bank tie-up, 'Prime' and 'Options 20', etc. have started yielding results. **Importantly, the brokerage segment is benefitting from tailwinds of increased trading activity from retail customers.** While distribution income has been weak this quarter, we attribute it to lower MF AUM coupled with the impact of the lockdown on non-MF distribution. This segment is likely to pick up gradually over the next few quarters. **The cost-cutting plan is on track – we expect C/I ratio to decline 440bp to 52% over FY20-23E. This should result in 19% PAT CAGR over FY20-23E.** We increase our estimates by ~17/13% for FY21/22. Maintain **Buy** with a TP of INR625 (24x FY22E EPS).

Quarterly Performance (INR m)

Y/E March	FY20				FY21				FY20	FY21E	1QFY21	Act v/s
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q			E	Est. (%)
Total Income	4,021	4,182	4,227	4,819	5,464	5,875	5,656	5,618	17,249	22,613	4,908	11
Change YoY (%)	-7.7	-8.7	4.4	12.5	35.9	40.5	33.8	16.6	-0.1	31.1	22.0	
Operating Expenses	2,261	2,341	2,376	2,742	2,870	3,189	3,051	3,078	9,720	12,188	2,674	7
Change YoY (%)	-3.1	-6.5	-3.7	14.5	26.9	36.2	28.4	12.2	0.2	25.4	18.2	
PBT	1,760	1,841	1,851	2,077	2,594	2,686	2,605	2,540	7,529	10,425	2,234	16
Change YoY (%)	-13.1	-11.4	17.1	10.0	47.4	45.9	40.7	22.3	-0.6	38.5	26.9	
Tax Provisions	622	490	479	519	663	691	670	655	2,109	2,679	559	19
Net Profit	1,138	1,351	1,372	1,559	1,931	1,995	1,935	1,885	5,420	7,746	1,676	15
Change YoY (%)	-15.0	0.7	35.6	28.3	69.7	47.7	41.0	20.9	10.4	42.9	47.3	
Key Operating Parameters (%)												
Cost to Income Ratio	56.2	56.0	56.2	56.9	52.5	54.3	53.9	54.8	56.4	53.9	54.5	
Tax Rate	35.4	26.6	25.9	25.0	25.6	25.7	25.7	25.8	28.0	25.7	25.0	
PAT Margins	28.3	32.3	32.5	32.3	35.3	34.0	34.2	33.6	31.4	34.3	34.1	
Revenue from Operations (INR Mn)												
Retail Brokerage Income	1,893	1,833	1,961	2,501	3,210				8,188			
Institutional Brokerage Income	306	326	285	372	348				1,289			
Investment Banking	167	323	176	99	223				765			
Distribution Income	984	1,062	1,029	1,155	798				4,230			
Other servicing Income	10	67	84	62	103				223			
Interest Income	501	535	602	712	624				2,350			
Other Operating Income	4	24	86	-96	154				17.7			
Revenue from Operations Mix (%)												
Retail Brokerage Income	49.0	44.0	46.4	52.1	58.8				48.0			
Institutional Brokerage Income	7.9	7.8	6.7	7.7	6.4				7.6			
Investment Banking	4.3	7.7	4.2	2.1	4.1				4.5			
Distribution Income	25.5	25.5	24.4	24.0	14.6				24.8			
Other servicing Income	0.3	1.6	2.0	1.3	1.9				1.3			
Interest Income	13.0	12.8	14.2	14.8	11.4				13.8			
Other Operating Income	0.1	0.6	2.0	-2.0	2.8				0.1			
Opex Mix (%)												
Employee Expenses	56.3	57.2	55.9	50.9	60.2				54.9			
Depreciation	6.9	6.3	6.2	5.9	4.7				6.3			
Interest Expenses	7.9	7.6	9.2	10.5	8.0				8.9			
Others	28.9	28.9	28.6	32.6	27.1				29.9			
Other Parameters (%)												
Blended MS	7.4	7.3	8.7	8.0	9.0							
Equity MS	8.1	8.7	8.9	9.1	10.7							
Derivatives MS	7.4	7.3	8.7	8.0	8.9							
NSE Active Customer MS	9.8	10.1	10.0	10.0	9.2							
No. Of Branches	192	187	178	172	171							
Network Patners	7500+	8000+	8600+	9400+	12100+							

Source: MOFSL, Company



Highlights from management commentary

Retail brokerage segment

- Rising retail participation in equity trading witnessed across the globe. This has been driven by activation of inactive clients as well as entry of new customers. WFH has also contributed to this phenomenon. Some of this participation may moderate in the coming quarters.
- **For the first 15 days of the quarter, the company did not open any accounts due to the lockdown as it did not have a fully-digital process. In addition, ICICI Bank itself was acquiring fewer new customers due to the lockdown – this, in turn, impacted ISEC.**
- **Launched 'ICICI Direct Insta' account which is the open-architecture platform. Customer acquisition happens digitally end-to-end. ISEC opened 20k such customer accounts in the quarter. This channel is now used for customers sourced by other means too.**
- Monthly average account opening increased YoY in June despite the lockdown. **ICICI Bank now contributes 65% of new account openings vs 80% earlier.**
- **In the equities business, the company witnessed 90% YoY increase in the number of customers trading on a daily basis.**
- Seeing share of delivery volumes going up. However, this may not be sustainable.
- **Employee expenses shot up this quarter due to high variable employee cost (due to strong company performance). Typically, 70% of an employee's total compensation is fixed.**
- Decline in other operating expenses this quarter was due to the one-time INR90m COVID provisions taken in 4QFY20 as well as due to renegotiation of some transaction and franking charges.
- 50% of retail brokerage business comes from 'Prime' customers.

Regulatory guidelines

- There is a SEBI regulation on collection of upfront margin in cash and derivative segments. There are also some changes in the margin requirement for these segments. There should not be any impact of the same on the cash market.
- There are also new guidelines in margin finance with respect to pledging and re-pledging of securities.
- SEBI regulation on intra-day margin collection – this will have some impact on the industry but it's too early to comment.
- While SEBI's guidelines are positive in the long term, there could be short-term challenges.

Distribution

- MF client base has bottomed out, though the SIP client base is still declining. ISEC's equity MF market share improved QoQ.
- Immediately post the closure of some schemes by an AMC, there were outflows from debt MFs. However, after some time, the company witnessed inflows back into fixed-income funds, but mostly in sovereign/AAA assets.

Capital markets

- Strong investment banking revenues were due to some large block trades as well as QIP mandates. This is likely to continue in 2Q too.

Others

- There is a clear trend towards preference towards online trading rather than trading through the physical format. This is true across all client segments.
- SEBI released simplified guidelines for digital on-boarding and KYC of customers which helped customers open accounts in the lockdown without any physical intervention.
- Focusing on digitizing all possible non-digital processes
- Focus is on growing the active client base from the current level of 1.5m
- **For the MTF book, ISEC borrows via CPs at ~5.5%. Average NIM is 4-5%. However, this book is likely to grow cyclically rather than structurally.**
- Outbound remittances from India amount to ~\$15b. But only \$500m is going into financial assets, while the rest is into physical & other assets/expenses.
- Activation rate is down QoQ due to the change in channel mix towards non-ICICI Bank channel customers.
- Under the open architecture, SBI and HDFCB are key channel contributors in addition to ICICI Bank.
- Covid provisions created last quarter have not been utilized. They are still on the balance sheet.
- ISEC has a PMS license, both for discretionary and non-discretionary. The AUM is ~INR1b (in an index fund).
- 70% of new customers acquired in the past four years are below the age of 30
- Improvement in yield this quarter is driven primarily by product mix (higher share of delivery in cash; lower share of derivatives)

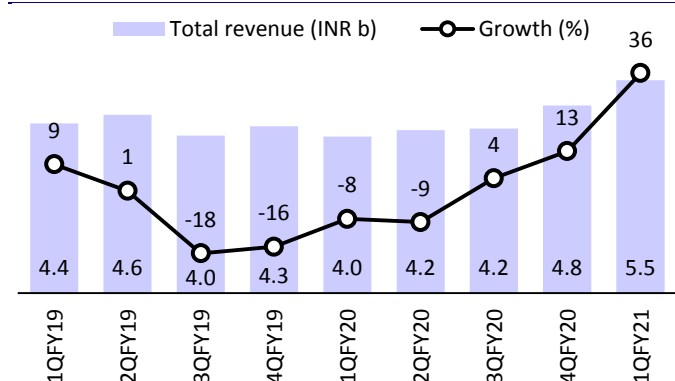
Valuation and view

- ISEC is a classic play on increasing the financialization of savings and retail participation in equity markets. Thus, its business and profitability is very cyclical.
- However, during the downcycle of the past two years, the company took several initiatives to make its business leaner and well-gearred for the upcycle. Initiatives such as the ICICI Bank tie-up, 'Prime', 'Prepaid' and 'Options 20' models, etc. have started yielding results. **Importantly, this segment is benefitting from tailwinds of increased trading activity from retail customers. ISEC is well-placed to benefit from sectoral tailwinds.**
- In the distribution segment, there have been regulatory headwinds in the past two years. However, with that now largely behind and notwithstanding near term challenges, revenue should improve gradually. We expect the company to maintain market share in mutual fund distribution. In the capital markets' segment, while ISEC is among the leading players, the business tends to be cyclical.
- Over FY20-23E, we expect revenue to grow at 14% CAGR, while cost-cutting should result in 440bp C/I ratio reduction. As a result, the company should deliver 19% PAT CAGR to INR9.2b. We increase our estimates by ~17/13% for FY21/22.
- Unlike the lending business, ISEC's business is largely capital light and the entire revenue is cash-flow based. Maintain **Buy** with a TP of INR625 (24x FY22E EPS).

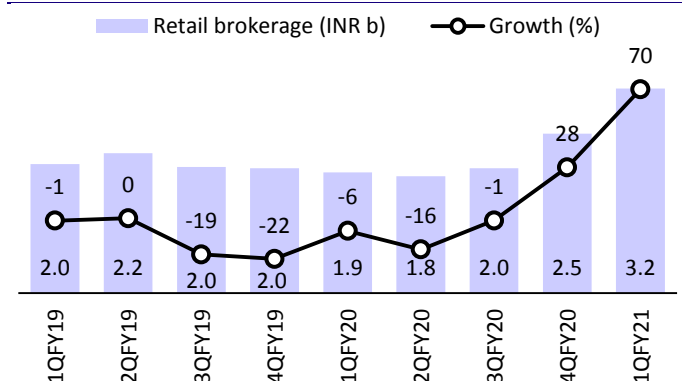
Exhibit 1: We upgrade estimates by ~15% to factor in stronger revenue growth in the brokerage segment

INR b	Old Est.		New Est.		Change (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Brokerage Income	11.3	12.4	14.5	13.9	28.4	11.8
Income from services	4.9	5.5	4.8	5.7	-2.7	4.1
Other Income	2.7	3.1	3.3	3.9	24.7	25.8
Total Income	18.9	21.0	22.6	23.5	19.8	11.9
Operating Expenses	10.1	11.0	12.2	12.1	21.1	10.2
PBT	8.8	10.0	10.4	11.4	18.3	13.7
Tax	2.2	2.5	2.7	2.9	21.6	14.9
PAT	6.6	7.5	7.7	8.5	17.2	13.4
C/I ratio	53.3	52.3	53.9	51.5		
RoE	50.5	49.4	58.4	54.3		
Dividend payout ratio	70.0	70.0	70.0	70.0		

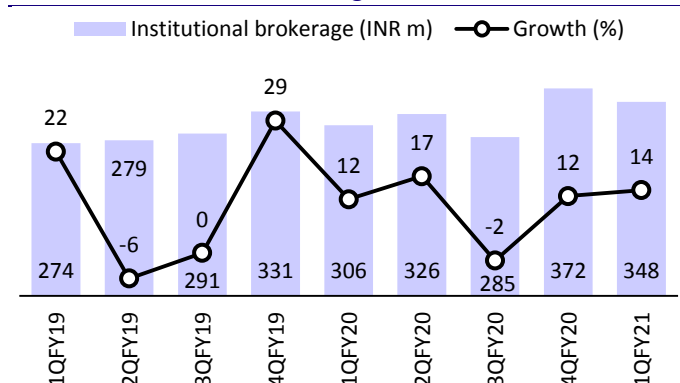
Source: MOFSL, Company

Key exhibits**Exhibit 2: Sharp pick-up in revenue growth...**

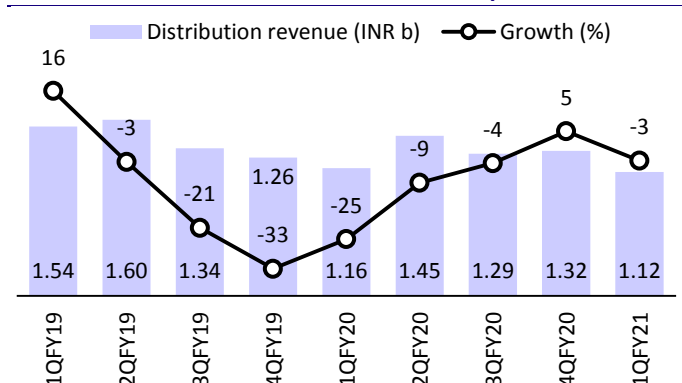
Source: MOFSL, Company

Exhibit 3: ...driven by retail brokerage

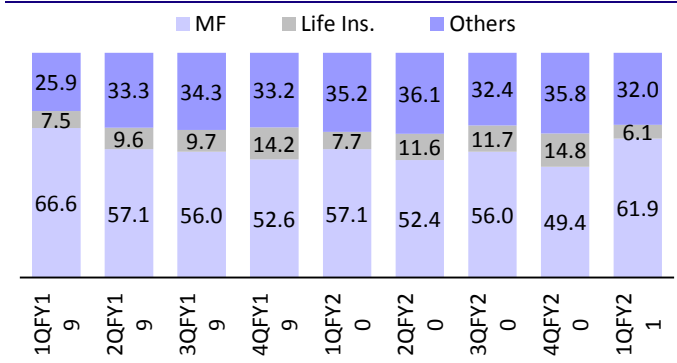
Source: MOFSL, Company

Exhibit 4: Institutional brokerage revenue trend stable...

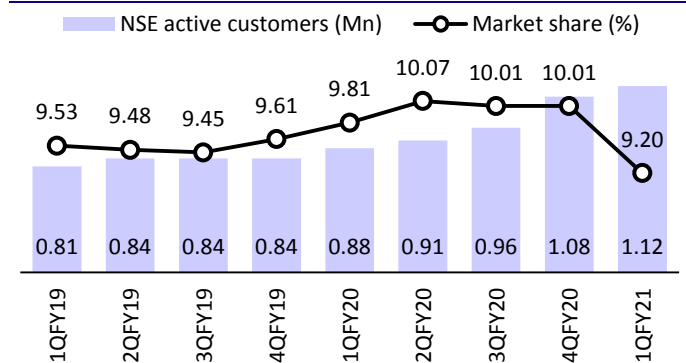
Source: MOFSL, Company

Exhibit 5: ...but distribution revenue under pressure

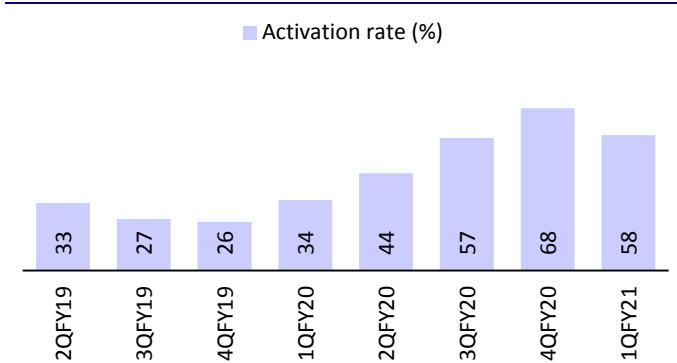
Source: MOFSL, Company

Exhibit 6: Mix of distribution revenue (%)

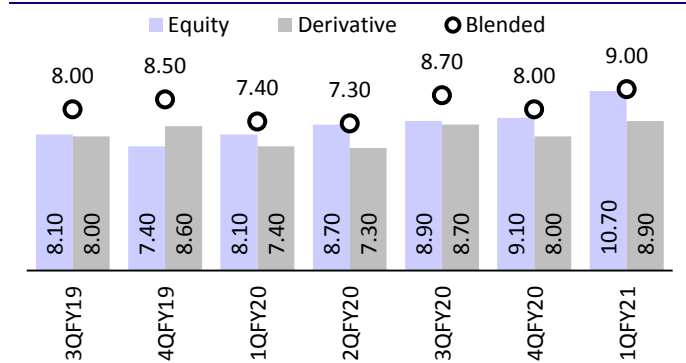
Source: MOFSL, Company

Exhibit 7: Dip in NSE active market share in the quarter due to lower account acquisitions

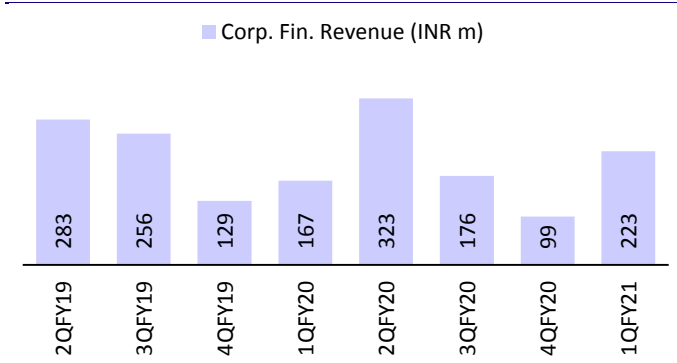
Source: MOFSL, Company

Exhibit 8: Marginal dip in activation rate (%) as channel excluding ICICI Bank gained traction

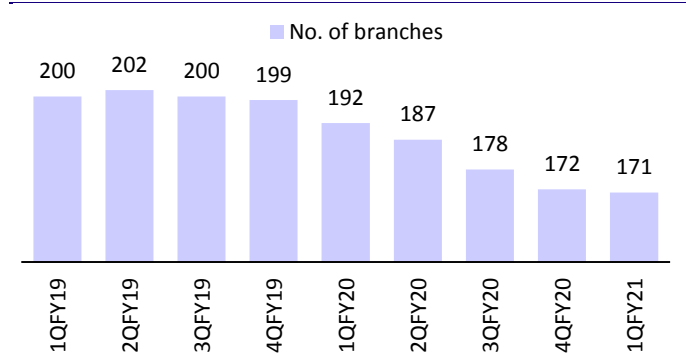
Source: MOFSL, Company

Exhibit 9: Market share up meaningfully in both segments

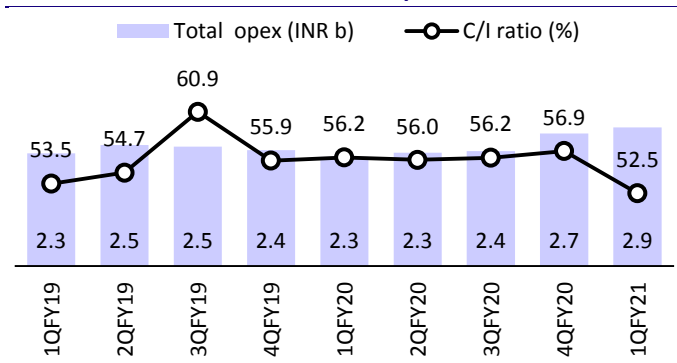
Source: MOFSL, Company

Exhibit 10: Investment banking revenue doubled QoQ

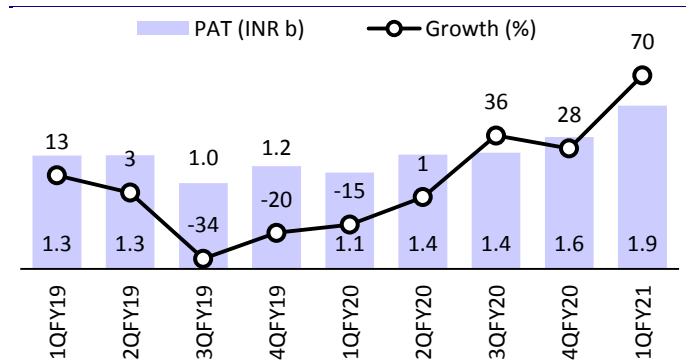
Source: MOFSL, Company

Exhibit 11: Branch rationalization ongoing

Source: MOFSL, Company

Exhibit 12: C/I ratio down 350-450bp QoQ and YoY

Source: MOFSL, Company

Exhibit 13: PAT jumps sharply due to strong revenue growth and lower tax rate YoY

Source: MOFSL, Company

Financials and valuations

Income Statement						(INR M)		
Y/E March	2016	2017	2018	2019	2020	2021E	2022E	2023E
Total Income	11,246	14,042	18,610	17,270	17,252	22,613	23,480	25,474
Change (%)	-7.0	24.9	32.5	-7.2	-0.1	31.1	3.8	8.5
Brokerage Income	6,607	7,756	10,243	9,328	9,477	14,519	13,864	14,628
Income from Services	3,499	4,982	6,552	5,733	5,218	4,753	5,711	6,310
Interest Income	957	1,091	1,574	1,792	2,350	2,996	3,446	3,963
Other Operating Income	182	214	241	193	20	325	435	545
Other Income	0	0	0	225	187	20	24	29
Operating Expenses	7,505	8,822	10,086	9,698	9,720	12,188	12,088	13,234
Change (%)	-1.2	17.6	14.3	-3.8	0.2	25.4	-0.8	9.5
Employee expenses	4,014	4,847	5,504	5,545	5,338	7,206	6,846	7,531
Interest expenses	258	289	495	423	864	1,166	1,341	1,543
Depreciation	160	155	153	150	614	564	589	614
Others	3,073	3,531	3,935	3,580	2,904	3,251	3,311	3,547
Profit Before Tax	3,741	5,220	8,524	7,572	7,532	10,425	11,392	12,241
Change (%)	-16.8	39.5	63.3	-11.2	-0.5	38.4	9.3	7.4
Tax	1,354	1,835	2,989	2,665	2,109	2,679	2,877	3,091
Tax Rate (%)	36.2	35.1	35.1	35.2	28.0	25.7	25.3	25.3
PAT	2,387	3,386	5,535	4,907	5,423	7,746	8,516	9,150
Change (%)	-18.8	41.8	63.5	-11.3	10.5	42.8	9.9	7.4
Proposed Dividend	1,939	2,468	3,646	3,646	3,736	5,422	5,961	6,405
Balance Sheet						(INR M)		
Y/E March	2016	2017	2018	2019	2020	2021E	2022E	2023E
Equity Share Capital	1,611	1,611	1,611	1,611	1,611	1,611	1,611	1,611
Reserves & Surplus	2,371	3,404	6,866	8,862	10,485	12,808	15,363	18,108
Net Worth	3,982	5,015	8,477	10,473	12,095	14,419	16,974	19,719
Borrowings	2,356	3,987	6,771	4,518	14,998	13,498	14,848	17,075
Other Liabilities	7,637	11,423	13,491	31,655	17,335	19,069	20,976	23,073
Total Liabilities	13,975	20,424	28,739	46,646	44,428	46,986	52,797	59,867
Cash and Investments	6,406	9,952	15,499	31,515	24,139	20,145	22,233	24,993
Change (%)	-25.0	55.3	55.7	103.3	-23.4	-16.5	10.4	12.4
Loans	1,546	50	5,782	4,033	5,709	10,847	13,016	15,619
Net Fixed Assets	378	375	421	476	2,061	2,267	2,494	2,743
Net Current Assets	5,644	10,048	7,037	10,623	12,520	13,727	15,054	16,512
Total Assets	13,975	20,424	28,739	46,646	44,428	46,986	52,797	59,867
E: MOFSL Estimates								

Financials and valuations

Ratios	(%)							
Y/E March	2016	2017	2018	2019	2020	2021E	2022E	2023E
As a percentage of Revenues								
Brokerage Income	58.8	55.2	55.0	54.0	54.9	64.2	59.0	57.4
Income from Services	31.1	35.5	35.2	33.2	30.2	21.0	24.3	24.8
Interest Income	8.5	7.8	8.5	10.4	13.6	13.3	14.7	15.6
Other Income	1.6	1.5	1.3	2.4	1.2	1.5	2.0	2.3
Total cost	66.7	62.8	54.2	56.2	56.3	53.9	51.5	51.9
Employee Cost	35.7	34.5	29.6	32.1	30.9	31.9	29.2	29.6
Opex (ex emp) Cost	31.0	28.3	24.6	24.0	25.4	22.0	22.3	22.4
PBT	33.3	37.2	45.8	43.8	43.7	46.1	48.5	48.1
PAT	21.2	24.1	29.7	28.4	31.4	34.3	36.3	35.9
Profitability Ratios (%)								
RoE	63.6	75.3	82.0	51.8	48.1	58.4	54.3	49.9
Dividend Payout Ratio	81.2	72.9	65.9	74.3	68.9	70.0	70.0	70.0
Valuations								
BVPS (INR)	12.4	15.6	26.3	32.5	37.5	44.8	52.7	61.2
Change (%)	13.0	25.9	69.0	23.5	15.5	19.2	17.7	16.2
Price-BV (x)					14.1	11.8	10.1	8.7
EPS (INR)	7.4	10.5	17.2	15.2	16.8	24.0	26.4	28.4
Change (%)	-18.8	41.8	63.5	-11.3	10.5	42.8	9.9	7.4
Price-Earnings (x)					31.5	22.0	20.0	18.7
DPS (INR)	5.0	6.4	9.4	9.4	10.9	16.8	18.5	19.9
Dividend Yield (%)					2.1	3.2	3.5	3.8
E: MOFSL Estimates								

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

*In case the recommendation given by the Research Analyst is inconsistent with the investment rating legend for a continuous period of 30 days, the Research Analyst shall within following 30 days take appropriate measures to make the recommendation consistent with the investment rating legend.

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