

Stock Update

IIFL Securities Ltd.

October 13, 2021





Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Capital Mkt Intermediary	Rs.112.4	Buy at LTP of Rs.112.4 & add more on dips of Rs.98	Rs.126	Rs.135.5	2 quarters

HDFC Scrip Code	IIFLSECEQ
BSE Code	542773
NSE Code	IIFLSEC
Bloomberg	IIFLSEC IN
CMP Oct 12, 2021	112.4
Equity Capital (Rs Cr)	60.6
Face Value (Rs)	2
Equity Share O/S (Cr)	30.29
Market Cap (Rs Cr)	3,407
Book Value (Rs)	32
Avg. 52 Wk Volumes	1341236
52 Week High	128.6
52 Week Low	36.5

Share holding Pattern % (Jun, 2021)	
Promoters	31.4
Institutions	48.3
Non Institutions	20.3
Total	100.0



HDFCsec Retail research
stock rating meter

for details about the ratings, refer at the end of the report

* Refer at the end for explanation on Risk Ratings

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Our Take:

IIFL Securities (IIFLSEC), belonging to the India Infoline group, is one of the key payers in the Indian financial services space offering a wide range of services including retail and institutional broking, financial products distribution, and investment banking. It is an established player with vast history and experienced management team. Also it has marquee investors like Fairfax group and other big institutional investors. The company has constantly endeavored towards the changing the revenue mix with higher focus on distribution revenue, which limits the risk of cyclicity and brings linearity. Technology and pricing-based disruptions are gradually changing the dynamics of the industry. The company is also constantly investing in technology and launching new innovative products to remain competitive with discount brokerages. The company has reported highest ever quarterly client addition at 1.5 lakh (includes Karvy customers) in Q1FY22. Also the company has started receiving encouraging response to its newly launched Z20 plan. We believe that the sale of land bank and continuous rise in customer acquisition, strong Investment Banking pipeline, growing financial products distribution revenue especially from Mutual fund will be the key triggers for the stocks re-rating.

We had issued Initiating Report on IIFLSEC on 28th June, 2021 and recommended Buy at LTP Rs.71.7 and add on dips to Rs. 63 band, for base case target of Rs.80.5 and bull case target of Rs.89 over the next two quarters. The bull case target of Rs.89 was achieved on 7th July 2021, yielding return of 24.2%.

Link for the Initiating Coverage:

<https://www.hdfcsec.com/hsl.research.pdf/IIFL%20Securities%20%20Ltd-Initiating%20Coverage-280621.pdf>

Valuation & Recommendation:

IIFLSEC has been able to stabilize its retail market share both in the cash and derivatives segments, despite the implementation of the third phase of peak margin norms. In FY21, owing to strong tailwinds across all capital market business IIFLSEC had delivered strong performance. Going forward, despite an expectation of higher volatility, we expect strong earnings growth to continue. We have envisaged 11% CAGR in top line and 13% in bottom line over FY21-FY23E. We expect dividend yield to improve to 3.7% in FY23E from current 2.3%. The stock is trading at a steep discount to its peers which we believe, will narrow gradually as the company has started gaining lost market share.



We feel that investors can buy IIFL Securities Limited at the LTP of Rs.112.4 (12.1x FY23E EPS) and add on dips to Rs.98 (10.5x FY23E EPS) band. We expect the Base case fair value of Rs.126 (13.5x FY23E EPS) and the Bull case fair value of Rs.135.5 (14.5x FY23E EPS) over the next 2 quarters.

Financial Summary

Particulars (Rs Cr)	Q1 FY22	Q1 FY21	YoY (%)	Q4 FY21	QoQ (%)	FY20	FY21	FY22E	FY23E
Total Income	251	150	67	238	5	790	868	959	1074
EBITDA	115	79	46	117	-1	357	380	425	482
RPAT	69	42	66	77	-11	132	220	244	283
EPS						7.3	7.0	8.1	9.3
RoE						29.1	23.9	23.2	23.1
RoCE						22.6	26.5	27.9	28.7
P/E						15.4	16.1	13.9	12.1
P/BV						4.0	3.5	3.0	2.6

(Source: Company, HDFC sec)

Recent Developments

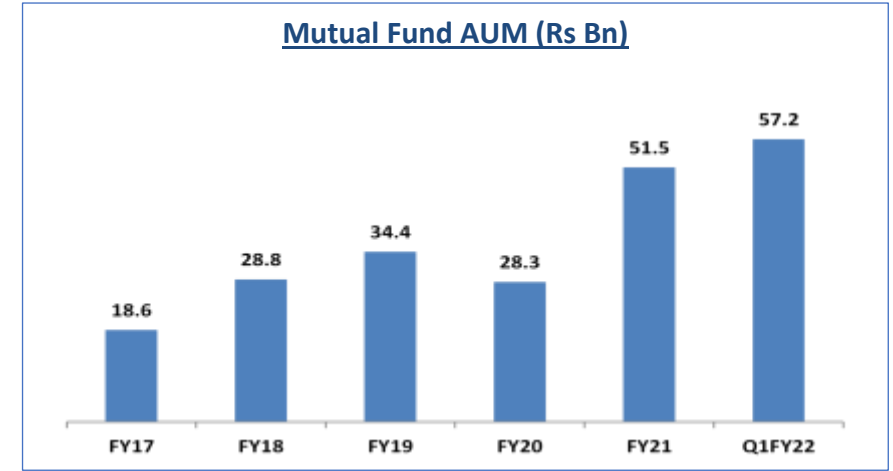
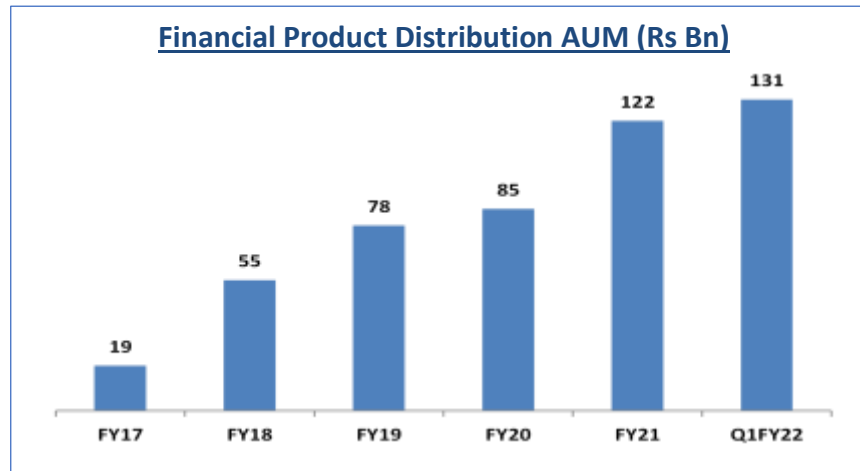
Q1FY22 Result Update

Consolidated revenues came at Rs.268 Cr, up 50% YoY and 5% QoQ. The brokerage income rose 40% to Rs.129.24 Cr. Investment banking income has increased manifold. Distribution income has increased almost 131% from Rs.21 Cr in the previous year to Rs.49 Cr this quarter, primarily driven by a combination of sale of high-yielding products like Portfolio Management Account etc., and also distribution of fixed income products like LCDs, MLDs, etc. It has lost market share in institutional broking business due to higher passive flows. The employee cost was up 5% QoQ and 42% YoY to Rs.66 Cr because of increase in headcount and salary hike. Net profit for the quarter stood at Rs.68.8 Cr, up 66% YoY and down by 11% QoQ.

Asset under management and custody stood at about Rs.55,141 Cr. It has reported highest quarterly client addition at 1.5 lakh (includes Karvy customers) in Q1FY22. Average daily turnover for the first quarter was Rs.52,791 Cr, which includes Rs.1,968 Cr in the cash segment and Rs.50,823 Cr of derivative segments. The corresponding figure for the Q4FY21 was Rs.44,153 Cr of which Rs.2,100 Cr in the cash segment and Rs.42,049 Cr in the derivative segment.



Distribution division update: The Company offers a wide range of products such as mutual funds, insurance, IPOs, bonds, AIF and others, targeting retail clients. Since the past couple of years, the management has shifted focus on distribution of retail financial products such as insurance and mutual funds. This strategy in the long term will create a granular revenue stream and help the company in hedging against the risk of cyclicity and volatility in capital markets. Financial products distribution AUM stood at Rs. 13,152 Cr. Insurance premium (Life + non-life) stood at Rs 29.3 Cr for the quarter, remained flat YoY. Mutual Fund AUM grew by 69% YoY and 11% QoQ to Rs 5,720 Cr as at June 30, 2021. SIP AUM grew by 65% YoY and 14% QoQ to Rs 1,163 Cr. IIFL Mutual Funds App (for Mutual Fund advisory, investments and investment management) is helping the company in steadily building on its customer base.



Positive macro lead indicators

FY2021 was a landmark year for the Indian capital markets with record number of demat accounts being opened and significant surge in equity and derivatives volume growth. This was led by historic volatility arising out of the pandemic, lower interest rate regime in the market and aided by work-from-home environment. The number of demat accounts opened increased from 5.0 mn in FY20 to 14.3 mn in FY21, a growth of 188% making this the year with highest number of demat accounts opened in any financial year till date. As of Q1FY22, further 7.1 mn demat accounts have been opened. The gross industry Average Daily Turnover or ADTO was up by 94% YoY. Contribution of retail participation to overall turnover was increased by ~300 bps in FY21. This trend shows that many young investors are getting attracted by the volatility and looking to trade/invest. In fact, India has a favourable demographic such as low penetration, rising household saving, increasing financial literacy etc. All these along with improving digital infrastructure bring vast opportunities. Digital natives comprising GenZ and Millennials are expected to increase by 15 mn - 20 mn annually for next 10 years (according to Census of India). This shows that a multiyear growth story is lying ahead of broking industry. Foreign Portfolio Investors (FPIs) flow also remained strong. There were a record high number of public offerings during the year. This continues even in FY22.



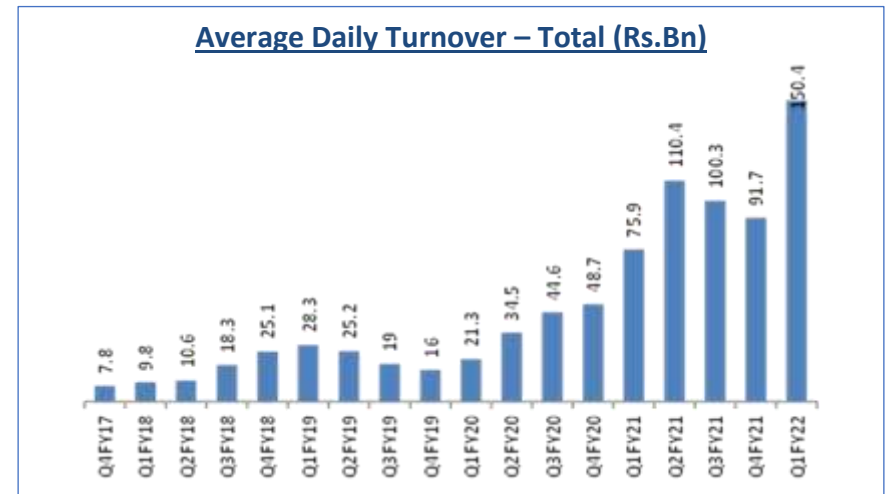
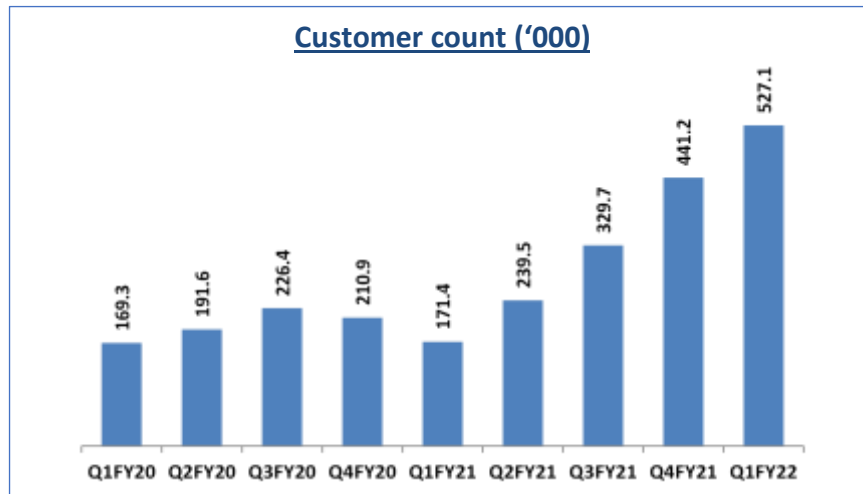
Worst impact of new margin rules is behind us

The new margin regulations came into force from December 2020. As a result of these norms, across the industry, there was some decline in turnover of derivative and intraday cash segment but it didn't impact revenue significantly, the same trend continues for the Phase-II and the impact was negligible in Phase-III (wef from Sept 01, 2021). Going forward, post the changes in regulatory margin requirements, in the non-discounted broking space, we expect consolidation in the industry and larger brokers with strong brand recall will have an edge over small and mid-sized brokerages.

Healthy customer acquisitions trend

The conscious efforts to acquire customers and continued investment in technology to make sure that the retail customers especially have a seamless trading experience, has resulted in strong client addition as well as rise in volumes. Karvy's demat account acquisition is also one of the contributors.

Recently the company has launched a new brokerage plan called Z20 where it offers a flat brokerage plan but that is completely DIY mode and where the company does not give any RM support. This is a pilot scheme, which can act as a means for both customer acquisition as well as retention tool. Management has informed that the company is seeing some amount of clients asking and coming back. However, they stated that this is just the added product in the portfolio, but the core focus will be a full-service brokerage.





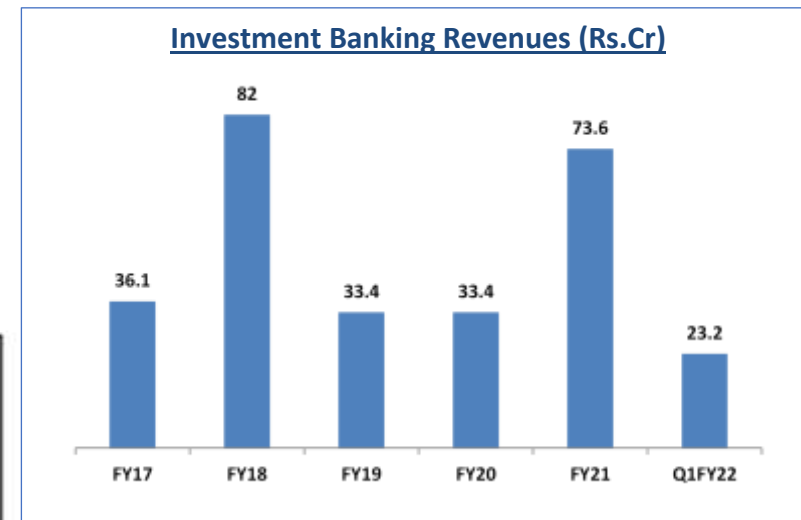
Land bank monetization

The company has about 6,16,000 square feet of property spread across many places Ahmadabad, Mumbai, Pune, Gurgaon, Hyderabad, Chennai, and it is carrying it at a cost of Rs.224 Cr and the market value will be about Rs.600 Cr. The management has informed that they are planning to monetise these properties; a bulk of this may be sold over the next few quarters to unlock value. Last quarter also they sold one big property. The exit from real estate will help the company lighten up the balance sheet which ultimately could bring upward rerating of IIFCSEC stock.

Investment banking business update

From FY21, the Investment Banking division has been into an uptrend with the overall bullish sentiment in the equity market. In Q1FY22, also the trend remains the same. The investment banking division completed 10 transactions including 4 IPOs, 4 QIPs and 2 private placement transactions. Management has further informed that the deal pipeline remains robust and they are running multiple transactions which are at various stages of execution. They feel that the company is well positioned to grow the segment given its superior research and strong distribution capabilities.

Transactions in Q1FY22





Major Tie-up

The company has been constantly doing tie ups with different players and fintech ecosystems to absorb future-ready technologies to achieve superior business results and leverage advancements in the evolving ecosystem. During the last quarter, the company has done two more tie ups to strengthen the offerings.

IIFLSEC has integrated with global investment platform Stockal for foreign investments. This partnership will help the customers in diversifying the portfolio in global assets. It will give access to over 3,500 US-listed companies, invest in fractional stocks, and expert-curated stocks and ETFs. It will appeal millennials customer base more. It has also partnered with safegold- a Digital Gold India Private Limited brand, to offer 999 fine 24 karat gold (99.99% pure). This partnership will help the customers purchase gold with a single click- just like stocks, mutual funds and debt products. Also they can get the instant loan on gold.

Risks & Concerns

- Capital market has inherent risk of volatility. The recent surge in the volume and retail participation could fade away with the some deep correction or sideways trend. And any prolonged period of negative returns from equity market can hit the company's revenues hard. However, the company is changing the revenue mix by bring in more distribution revenue, which negates risk of cyclical to some extent.
- Any adverse change of regulation or non-compliance of rules might impact the company's growth.
- The broking industry is currently facing significant pressures on account of increased competition from discount brokers. Also the discount brokers have a disproportionately high share in new acquisition of clients, though it has not yet shown up in terms of topline or ARPUs for most discount brokers. While the capital market cycle has been positive and volumes have compensated for declining yields, a reversal of investments into financial assets will have a significantly negative impact on both asset prices and trading volumes, which in turn will significantly impair broking revenues and earnings. Also the new plans introduced by the company (Z20) to attract /retain clients could lead to fall in yields and if ARPUs don't rise, then it could hit margins.
- Any delay or failure in transitioning Karvy demat accounts can impact their future growth and margins.
- As compared to other listed and non-listed brokers, IIFL sec has to catch up with digitization of customer interface. Also the dependence on broking income is higher in the case of IIFL sec that reflects into lower valuation being ascribed to them. However it is working at a fast pace to correct these shortcomings and hence the discount in valuation could narrow over time.



Company Background:

IIFL Securities Ltd is one of the key capital market players in the Indian financial services space. IIFL Securities along with its subsidiaries offers advisory and broking services, financial products distribution, institutional research and investment banking services. IIFL Securities has established itself through a combination of leading-edge technology, diverse product offerings, management expertise, and a wide network of branches across India. The Company has developed long-term relationships with its customers with sustained high quality performance and continues to be their preferred investment partner.

Peer comparisons

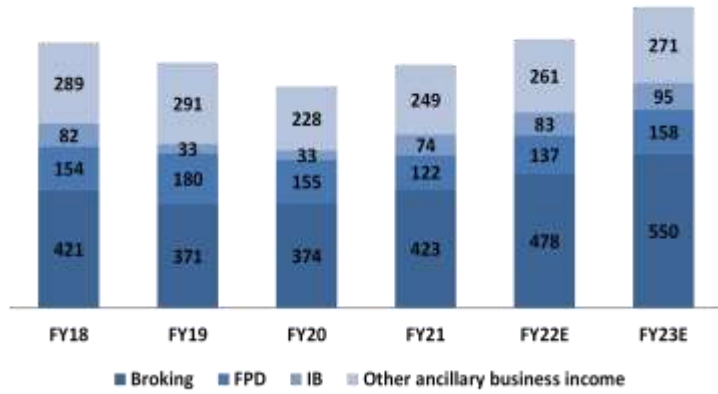
	CMP	Mcap (Rs bn)	FY21 (Rs bn)				EPS			P/E		
			Sales	NP	Margin (%)	RoE(%)	FY21	FY22	FY23	FY21	FY22	FY23
ICICI Securities	843.9	272.2	24.3	10.7	59.1	70.4	33.1	32	31.7	25.5	26.4	26.6
IIFL Securities	112.4	34.07	8.7	2.2	48.1	23.9	7	8.1	9.3	16.1	13.9	12.1
Angel Broking	1447.3	119.6	9.0	3.1	47.9	35.6	37.5	42.8	50	38.6	33.8	28.9

Active clients and market share of top players as on August 2021

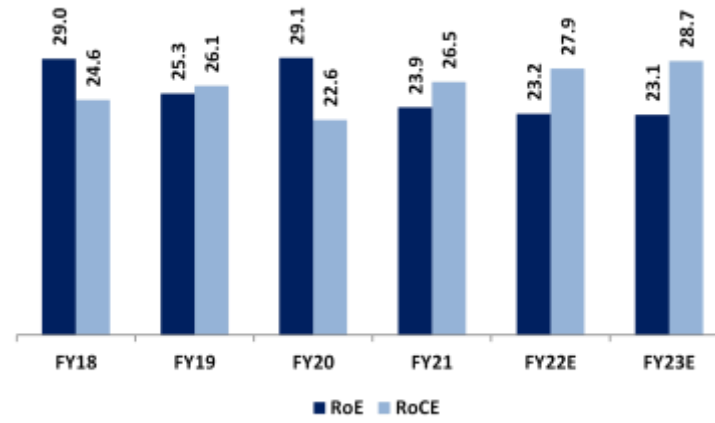
Sr No	Name of Stockbroker	Active Clients	Market Share (%)
1	ZERODHA BROKING LIMITED	3602074	19.6
2	RKSV SECURITIES INDIA PRIVATE LIMITED	2141095	11.7
3	ICICI SECURITIES LIMITED	1580233	8.6
4	ANGEL BROKING LIMITED	1564667	8.5
5	HDFC SECURITIES LTD.	957085	5.2
6	SPAISA CAPITAL LIMITED	870405	4.7
7	NEXTBILLION TECHNOLOGY PRIVATE LIMITED	780570	4.3
8	KOTAK SECURITIES LTD.	743206	4.0
9	SHAREKHAN LTD.	679333	3.7
10	MOTILAL OSWAL FINANCIAL SERVICES LIMITED	564034	3.1
11	AXIS SECURITIES LIMITED	454882	2.5
12	SBICAP SECURITIES LIMITED	329099	1.8
13	IIFL SECURITIES LIMITED	291730	1.6
14	GEOJIT FINANCIAL SERVICES LIMITED	201206	1.1



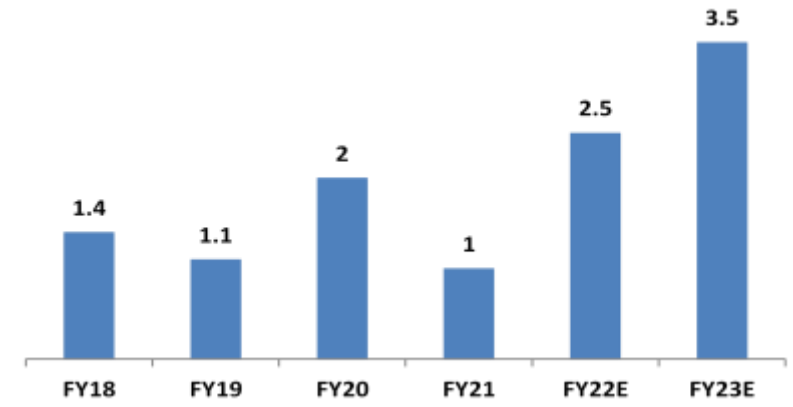
Revenue mix %



Return Ratios(%)



DPS (Rs.)





Financials

Income Statement

(Rs Cr)	FY19	FY20	FY21	FY22E	FY23E
Total Income	876	790	868	959	1074
Growth (%)	-7.6	-9.8	9.8	10.6	12.0
Operating Expenses	458	433	488	534	592
EBITDA	418	357	380	425	482
Growth (%)	-9.2	-14.6	6.4	11.9	13.4
EBITDA Margin (%)	50.1	49.3	48.1	48.6	49.2
Depreciation	41.9	55.3	45.9	47.0	49.0
EBIT	376	302	334	378	433
Interest	114.5	102.1	49.6	53.1	56.5
PBT	262	200	285	325	377
Tax	86.6	67.5	64.4	81.3	94.2
PAT	175	132	220	244	283
EPS	5.4	7.3	7.0	8.1	9.3

Balance Sheet

(Rs Cr)	FY19	FY20	FY21	FY22E	FY23E
SOURCE OF FUNDS					
Share Capital	63.8	63.9	60.6	60.6	60.6
Reserves	667	816	907	1075	1252
Shareholders' Funds	731	880	968	1136	1312
Long-Term Borrowings	709	459	292	219	197
Total Source of Funds	1440	1338	1259	1354	1509
APPLICATION OF FUNDS					
Net Block	388	393	394	348	309
Capital Work-in-Progress	86	130	132	142	155
Non-Current Investments	5	9	9	10	12
Deferred Tax Assets (net)	46	20	21	21	21
Long Term Loans & Advances	1042	471	1085	1162	1276
Total Non-Current Assets	1567	1023	1642	1684	1774
Current Investments	275	231	104	113	126
Inventories	0	13	2	2	2
Trade Receivables	33	39	45	48	52
Cash & Equivalents	1065	1027	1678	1936	2176
Other Current Assets	110	100	73	79	87
Total Current Assets	1483	1410	1903	2179	2443
Short-Term Borrowings	1348	1020	2214	2436	2631
Trade Payables	27	37	41	46	51
Other Current Liab & Provisions	235	38	29	27	26
Total Current Liabilities	1610	1095	2285	2508	2708
Net Current Assets	-127	315	-382	-329	-264
Total Application of Funds	1440	1338	1259	1354	1509

(Source: Company, HDFC sec)



Cash Flow Statement

(Rs Cr)	FY19	FY20	FY21	FY22E	FY23E
Reported PBT	258	301	285	325	377
Non-operating & EO items	-734	-696	-232	-84	-93
Interest Expenses	114	102	50	53	57
Depreciation	42	55	46	47	49
Working Capital Change	287	-493	1,358	205	175
Tax Paid	-87	-68	-64	-81	-94
OPERATING CASH FLOW (a)	-119	-797	1,442	465	470
Capex	85	-39	-3	-5	-10
Free Cash Flow	-34	-836	1,439	460	460
Investments	86	592	-615	-78	-116
Non-operating income	40	66	77	84	93
INVESTING CASH FLOW (b)	211	619	-541	1	-33
Debt Issuance / (Repaid)	-388	-250	-167	-73	-22
Interest Expenses	-114	-102	-50	-53	-57
FCFE	-537	-1,188	1,222	334	382
Share Capital Issuance	0	0	-3	0	0
Dividend	-35	-64	-30	-76	-106
FINANCING CASH FLOW (c)	-537	-416	-250	-202	-184
NET CASH FLOW (a+b+c)	-445	-594	650	264	253

Key Ratios

	FY19	FY20	FY21	FY22E	FY23E
Profitability (%)					
EBITDA Margin	50.1	49.3	48.1	48.6	49.2
EBIT Margin	45.0	41.7	42.3	43.2	44.2
APAT Margin	20.5	32.3	27.9	27.9	28.8
RoE	25.3	29.1	23.9	23.2	23.1
RoCE	26.1	22.6	26.5	27.9	28.7
Solvency Ratio					
D/E	2.8	1.7	2.6	2.3	2.2
Net D/E	1.0	0.3	0.7	0.5	0.4
PER SHARE DATA					
EPS	5.4	7.3	7.0	8.1	9.3
BV	23	28	32	37	43
Dividend	1.1	2.0	1.0	2.5	3.5
VALUATION					
P/E	20.8	15.4	16.1	13.9	12.1
Dividend Yield	1.0	1.8	0.9	2.2	3.1
P/BV	4.9	4.0	3.5	3.0	2.6
EV/EBITDA	9.7	11.3	10.7	9.5	8.4

One Year Price Chart





HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicity of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

Disclosure:

I, **Nisha Sankhala, (MBA)**, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. HSL has no material adverse disciplinary history as on the date of publication of this report. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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