

Near-term Headwinds Persist; Focus Remains on Gaining Market Share!

ICICI Securities' (ISEC) Q2FY23 performance was marginally ahead of our estimates, driven by better-than-expected broking income. The broking industry witnessed sustained growth momentum in derivative volumes (+25% QoQ), though cash volumes remained flat QoQ (the silver lining being the halt in the sequential de-growth witnessed for 5 consecutive quarters). ISEC registered flat growth in broking and allied revenues, highlighting the company's efforts to reduce the share of cyclical components. However, core broking revenues (retail + insti.) continued to de-grow by 16% YoY, with cash ADTO declining substantially by ~21% YoY. Distribution income continued to support revenue growth, though remained tepid growing at 5/3% YoY. The mix of distribution revenues improved to 18% vs 17% QoQ.

The company's revenue stood at Rs 858 Cr (flat YoY, +8% QoQ), marginally ahead of our expectations of Rs 821 Cr. With headwinds limiting the topline growth, ISEC channelized its focus on rationalizing Opex even as it continued to invest in technology, analytics, marketing, and hiring talent to build a future ready franchise to harness long-term growth opportunities. However, owing to a muted topline growth, the C-I Ratio remains optically elevated at 53.4% vs 45/53.8% YoY/QoQ. PAT stood at Rs 300 Cr (vs our expectations of Rs 289 Cr; -14% YoY, +10% QoQ).

Q2FY23 witnessed some revival in certain key industry parameters with the industry recording a strong 25% QoQ increase in derivative ADTO and improved SIP flow increasing by 4% QoQ. However, on the flip side, the new demat account openings moderated by 25% QoQ, NSE active users declined and primary market activity remained muted. Macro headwinds continue to persist and will continue to pose challenges on the revenue (especially broking) and profitability front in the near term.

Key Result Highlights

- Moderation in Customer sourcing momentum** – ISEC added 462K customers (vs. 583K customers YoY and 447K customers QoQ) during Q2FY23 taking the client base to ~8.4 Mn customers (+34% YoY). Total active clients stood at 3.46 Mn (+34% YoY, -3% QoQ), while NSE active clients stood at 3.06 Mn (+35% YoY, -4% QoQ). In-line with industry, ISEC witnessed moderation in active client base, and lost ~20bps on NSE active market share QoQ.
- Improving Cross-sell** – Led by a superior product proposition, the number of clients having 2+ products improved to 1.19 Mn vs. 1.09/1.17 Mn YoY/QoQ.

Management Concall Key Takeaways

Key Focus areas identified – With near-term headwinds persisting, ISEC has identified 4 key levers to ensure sustainable growth over the medium to long term - (a) Improving market share across segments, (b) Diversifying the revenue mix to reduce the impact of cyclicity on revenues, with added focus on the wealth management vertical, (c) Undertaking cost optimization measures, and (d) Strengthening product pipeline.

Valuation and Recommendation

With efforts to gain market share finally yielding results in both the cash and derivative segment, we expect marginal revival in broking revenues in H2FY23. With distribution income from MFs and Insurance being pronounced in H2, we expect some recovery in revenue growth in H2FY23. As the company progresses on further diversifying its revenue streams by scaling up the distribution income, it will help partially off-set the pressure on broking revenues. ISEC will continue to invest in technology and franchise strengthening to ensure sustainable growth over the long term, thereby keep cost ratios elevated in the near term. Backed by improving market share aiding broking revenues, continuous enhancement of the distribution product suite along with the ramp up of the wealth vertical is likely to support revenue growth we revise our revenue estimates by 2-8% over FY23-25E. With operating leverage kicking-in we expect traction on earnings to improve and hence we revise our earnings estimates upwards by 2-9% over FY23-25E. **As valuations are inexpensive (11x FY24E EPS vs long-term avg. P/E of ~15x), we continue to maintain our BUY recommendation on the stock with a revised target price of Rs 625/share (14x FY24E EPS), implying an upside of 23% from the CMP.**

Key Financials (Consolidated)

(Rs. Cr)	FY22	FY23E	FY24E	FY25E
Revenues	3,435	3,553	3,975	4,449
PBT	1,853	1,666	1,925	2,192
PAT	1,383	1,246	1,440	1,639
EPS (Rs)	42.8	38.6	44.6	50.8
EPS Growth (%)	29%	-10%	16%	14%
P/E (x)	11.8	13.1	11.4	10.0
Div. Payout (%)	56%	55%	55%	55%
RoE (%)	65.0%	46.0%	43.4%	40.9%

Source: Company, Axis Research

(CMP as of Oct 20, 2022)

CMP (Rs)	507
Upside /Downside (%)	23%
High/Low (Rs)	886/408
Market cap (Cr)	16,354
Avg. daily vol. (6m) Shrs.	4,40,322
No. of shares (Cr)	32.3

Shareholding (%)

	Jun-22	Mar-22	Dec-21
Promoter	74.9	74.9	74.9
FII	7.1	7.3	6.6
MFs	2.1	2.6	3.1
Others	15.9	15.2	15.4

Financial & Valuations

Y/E Mar (Rs. Cr)	FY23E	FY24E	FY25E
Revenues	3,553	3,975	4,449
PBT	1,666	1,925	2,192
PAT	1,246	1,440	1,639
EPS (Rs)	38.6	44.6	50.8
EPS Growth (%)	-10%	16%	14%
P/E (x)	13.1	11.4	10.0
Div. Payout (%)	55%	55%	55%
ROE (%)	46.0%	43.4%	40.9%

Change in Estimates (%)

Y/E Mar	FY23E	FY24E	FY25E
Revenues	2.3	7.9	7.7
PBT	1.5	9.0	3.8
PAT	1.5	9.0	3.8

Axis vs Consensus

EPS Estimates	FY23E	FY24E	FY25E
Axis	38.6	44.6	50.8
Consensus	34.6	39.5	42.0
Mean Consensus TP (12M)			538

ESG disclosure Score**

Environmental Disclosure	15.2
Social Disclosure Score	25.2
Governance Disclosure Score	78.6
Total ESG Disclosure Score	39.7

Source: Bloomberg, Scale: 0.1-100

**Note: This score measures the amount of ESG data a company reports publicly, and does not measure the company's performance on any data point. All scores are based on 2021 disclosures

Relative performance



Source: Capitaline, Axis Securities

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Additional Concall Highlights (Contd...)

- **Market share gains visible across segments** – ISEC's efforts continued to yield results with market share gain visible across segments. In the retail derivative segment, the company gained market share by ~20bps to 3.7% vs 3.5% QoQ for the second consecutive quarter. With the company's focused approach having identified 4-lever to gain market share, ISEC has also seen an improvement in the no. of customers and order count.

Similarly, in the retail equity segment, the company's market share improved from 9.7% in Q1FY23 to 10.6% in Q2FY23. The leadership in the MTF book continued with the company commanding a market share of 23% vs 21.8/22.4% YoY/QoQ. The recently launched commodity trading segment continues to perform well and gain market share, which stood at 5.5% vs 4.4% QoQ.

- **Diversifying revenue streams to help counter cyclicality** – As capital market sentiments remained weak with primary issuances drying up, ISEC focused efforts on building a strong pipeline of Rs 54,000 Cr across 28 deals and is also engaging in more deals. It currently has 16 mandates for IPOs in its kitty, the amount for which is yet to be ascertained. More clarity will emerge on the same as market sentiments improve and the strong deal pipeline will resultantly translate into strong revenue growth in the issuer segment.

Similarly, in the allied revenues, the company has introduced charges on 'Prime' and 'NEO' (Call and Trade charges, Demat charges, fund transfer charges etc.) which has started picking up and will contribute to revenue growth. During the quarter, allied income grew by 45% YoY led by the MTF and Prime Fees.

Furthermore, in the distribution vertical, Mutual Funds and Insurance will remain key growth drivers. The company will also look to scale-up the loan distribution and insurance to support revenue growth. Along with loan disbursements, Fixed income products also continue to witness good traction. During the quarter, SIP flows (avg. quarterly run-rate of Rs 400-420 Cr) moderated QoQ owing to changes in regulatory requirements impacting the flows. However, the management remains confident of the company's ability to maintain its competitive position in the SIP market.

- **Wealth Management business offers greater potential to scale up** – In its endeavor to granularize revenues, the wealth management vertical offers ample scope for growth. The vertical, a proposition for HNI customers, offers better customer persistency in terms of customer retention, average revenues and AUMs. Trends suggest that increasing vintage of the customer aid revenue and ARPU growth amongst the wealth customers. The approach in this segment remains customer centric, with ISEC looking to on-board clients (quarterly run-rate of 1500-3000 customers) and maximize AUMs through improved engagement to facilitate growth. The vertical has a dedicated team of ~500 members who continue to engage with the customer through multiple channels.
- **New client addition to be selective** – In H1FY23 the new client addition run-rate has averaged at 450-460K customers per quarter. With the industry facing headwinds in terms of new client additions, ISEC will choose to remain selective in its approach in sourcing new customers. ***The approach will be focused on sourcing customers from channel with higher potential to generate revenues and will aim to maintain a market share of 7-7.5% in the incremental demat account sourcing.***

Change in Estimates

	Revised			Old			% Change		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenues	3,558	3,980	4,455	3,477	3,688	4,154	2.3	7.9	7.2
PBT	1,666	1,925	2,192	1,642	1,767	2,110	1.5	9.0	3.8
PAT	1,246	1,440	1,639	1,228	1,321	1,578	1.5	9.0	3.8

Source: Axis Securities

Result Update (Consolidated)

	Q2FY23	Q2FY22	YoY %	Q1FY23	QoQ %
Business Metrics					
Client Base (Mn)	8.0	5.8	37.2	7.6	5.0
Client Addition ('000)	447	389		618	
Overall Active clients	3.6	2.2	62.6	3.4	5.0
NSE Active clients	3.2	1.9	72.4	3.0	5.3
ISEC Total ADTO	1,582	838	88.7	1,379	14.7
Market share	2.9%	3.4%		2.8%	
Equity Segment ADTO (calc.)	35	52	-33.2	43	-19.3
Equity Segment Market Share	8.0%	9.2%		8.9%	
Derivative Segment ADTO (calc.)	1,547	786	96.8	1,336	15.8
Derivative Segment Market Share	2.9%	3.3%		2.8%	
Wealth Management AUMs (Rs Bn)	2,777	2,009	38.2	2,858	-2.8
MF AUM (Rs. Trn)	489	440	11.1	503	-2.8
Life Insurance Premium (Cr)	135	125	8.3	296	-54.3
Profit & Loss					
Revenue from Operations	777	737	5.3	872	-10.9
-- Broking Income	303	395	-23.2	373	-18.6
-- Income from Services	255	211	21.2	287	-11.2
-- Interest Income	218	132	65.5	212	2.9
Other Operating Revenues	17	8	113.1	19	-13.7
Other Income	1	2	-49.6	1	92.1
Total Revenue	795	748	6.3	892	-10.9
Operating Expenses					
-- Employee Expenses	175	151	16.0	172	1.5
-- Interest Expense	100	42	140.2	91	10.2
-- Depreciation	16	14	13.9	17	-5.5
-- Other Opex	136	124	9.7	156	-13.0
Total Expenses	428	331	29.2	437	-2.1
C-I Ratio (%)	53.8%	44.3%		49.0%	
EBITDA	483	471	2.6	563	-14.3
EBITDA Margin (%)	60.7%	62.9%		63.1%	
Profit Before Tax	367	417	-11.9	455	-19.4
Tax	93	106	-11.8	115	-18.8
Profit After Tax	274	311	-11.9	340	-19.6

Source: Company, Axis Securities

Financials (Consolidated)

Profit & Loss

(Rs Cr)

Y/E March	FY22	FY23E	FY24E	FY25E
Revenue from Operations	3,435	3,553	3,975	4,449
Other Income	4	5	6	7
Net Income	3,438	3,558	3,980	4,455
<i>Change %</i>	33%	3%	12%	12%
Total Operating Expense	1,586	1,892	2,055	2,264
PBT	1,853	1,666	1,925	2,192
Tax	470	420	485	553
Profit After Tax	1,383	1,246	1,440	1,639
<i>Change</i>	29%	-10%	16%	14%

Source: Company, Axis Securities

Balance Sheet

(Rs Cr)

Y/E March	FY22	FY23E	FY24E	FY25E
Equity Share Capital	161	161	161	161
Reserves & Surplus	2,269	2,830	3,478	4,215
Net Worth	2,431	2,991	3,639	4,377
Borrowings	7,846	9,022	10,376	11,932
Other Liabilities	3,370	3,640	3,931	4,245
Total Liabilities	13,646	15,653	17,946	20,554
Cash & Bank balances	5,617	6,731	7,797	9,001
Loans	6,857	7,679	8,831	10,156
Fixed Assets & Others	1,173	1,243	1,318	1,397
Total Assets	13,646	15,653	17,946	20,554

Source: Company, Axis Securities

Ratio Analysis

(%)

Y/E March	FY22	FY23E	FY24E	FY25E
Profitability & Efficiency Ratios				
RoE	65.0%	46.0%	43.4%	40.9%
RoA	12.7%	8.5%	8.6%	8.5%
Cost to Income	46.2%	53.2%	51.7%	50.9%
Valuation				
BVPS	75.3	92.7	112.8	135.6
Change	33%	23%	22%	20%
Price-BV (x)	6.7	5.5	4.5	3.7
EPS	42.8	38.6	44.6	50.8
Change	29%	-10%	16%	14%
Price-Earnings (x)	11.8	13.1	11.4	10.0
Dividend Per Share	24.0	21.2	24.5	27.9
Dividend Payout Ratio	56%	55%	55%	55%
Dividend Yield (%)	4.7%	4.2%	4.8%	5.5%

Source: Company, Axis Securities

ICICI Securities Price Chart and Recommendation History



Date	Reco	TP	Research
13-Sep-21	Buy	870	Initiating Coverage
28-Sep-21	Buy	870	Company Update
20-Oct-21	Buy	940	Result Update
19-Jan-22	Buy	990	Result Update
21-Apr-22	Buy	865	Result Update
22-Jul-22	Buy	575	Result Update
21-Oct-22	Buy	625	Result Update

Source: Axis Securities

About the Analyst



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