SMC Global Securities Limited

March 01, 2021

Ratings

Facilities	**Amount (Rs. crore)**	**Rating[1]**	**Rating Action**
Commercial Paper	25 (Rupees Twenty Five Crore Only)	CARE A1+ (A One Plus)	Reaffirmed

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

CARE has based its assessment of SMC Global Securities Ltd (SMC) on the combined view of SMC Global Securities Ltd (SMC) and its subsidiaries (together called the SMC Group).

The reaffirmation of ratings takes into consideration the experienced promoters and management team, long track record of operations of SMC group in the capital markets segment with established brand and market position, wide franchisee network and large client base and diversified product profile leading to diversified earnings of the group. The rating also derives strength from risk management systems in place, comfortable gearing levels of the group and comfortable liquidity position at parent entity level supported by arbitrage book of Rs.115 crore which can be liquidated in case of need. Also, the rating of SMC Global Securities taken into account healthy level of margin utilization with exchanges.

These rating strengths are, however, partially off-set by the volatility in earnings and thin broking margins associated with capital markets although it has been noticed that the dependence on the same has gradually reduced over the years with increasing presence in lending business (NBFC) and other products which are less susceptible to capital market conditions. The ratings are also constrained on account of market risk owing to significant proprietary trading book, however, most trades are hedged and algo-based and there is established track record of consistent stable profits in arbitrage book. Also, the group's profitability moderated in FY 20 with return of total assets (RoTA) and return on net worth (RoNW) at 1.15% and 3.74% respectively as on March-20 and 4.36% and 13.32% (annualized) respectively as on Dec-20 as against 3.67% and 12.33% respectively end FY19. Also, the NBFC lending book is yet to season fully and asset quality indicators, though under pressure, remain manageable thus far.

Going forward, the ability of the group to profitably grow its operations while maintaining adequate risk management systems, thereby limiting credit losses in broking, trading and lending businesses, maintaining a comfortable capital structure and liquidity position coupled with improvement in asset quality in its NBFC operations would be the key rating sensitivities.

<u>Rating Sensitivities</u>

Positive Factors - Factors that could lead to positive rating action/upgrade:

- Further diversification of the income and profitability profile with reduction in reliance on the capital markets
- Scale up of operations and improvement in profitability indicators across segments with RONW greater than 10% on a sustained basis
- Raise funding from diverse sources for the lending business at competitive costs

Negative Factors- Factors that could lead to negative rating action/downgrade:

- Deterioration in asset quality at NBFC level or credit losses in the broking segment thereby impacting the profitability and capitalization levels
- Increase in adjusted net gearing levels beyond 4 times
- Decline in cash surplus and liquidity buffers which could impact the risk absorption ability

Detailed description of the key rating drivers

[1]*Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

Key Rating Strengths

Experienced promoters and management team

The group is promoted by first generation entrepreneurs, Mr. Subhash C. Aggarwal (Chairman and MD) and Mr. Mahesh C. Gupta (Vice-Chairman and MD). Both the promoters are Chartered Accountant by qualification and have more than 35 years of diverse experience in financial services and securities market. The company has a strong and experienced Board of 12 members, including 6 Independent Directors. SMC group is well supported by a strong management team having rich experience in their respective fields to support the various businesses.

Long track record of operations with established brand

SMC Group was incorporated in December 1994 and has more than two decades of track record of operations in the equity broking business. The group diversified into commodity broking in 2003, insurance broking in 2006 and NBFC business in 2008. The company also has international presence through its subsidiary in Dubai (for commodity trading on DGCX). Over the years, the group has established its brand, in the broking, advisory and financial product distribution businesses. Given its track record and established brand, the company has been able to enter into various strategic partnerships including being the preferred insurance broker for Honda cars under Honda Assure, for KIA cars with KIA motors, preferred broker for PNB providing trading facilities and demat services etc. Further, SMC has launched its own discount broking platform in order to cater to the larger segment that prefers online trading. Also, shares of SMC got listed on NSE and BSE on 24th February 2021.

Wide branch network with large franchisee network and client base

SMC has a strong pan India presence through its network of around 95 branches and 2500+ sub-brokers and 13,700+ independent distributors as on Dec 31, 2020. SMC has a client base of around 18 lacs which includes largely retail customers and few institutional customers with most of the brokerage income (equity, commodity and currency) coming from retail customers. SMC leverages its wide network for distribution of various financial products (Mutual Funds, Insurance, Debt, etc.).

Diversified product profile albeit stagnant share of the lending business (NBFC)

The group has presence in broking, depositary services, proprietary trading, distribution of financial products (Mutual Funds, Insurance, Debt instruments, IPO, etc.), lending operations, portfolio management services (PMS) and Wealth management, real estate broking and advisory services and investment banking. Furthermore, within broking, the company has a well-diversified product profile with presence in equity, derivatives, currency and commodity.

During 9M FY21, the broking income accounted for 53% of total income followed by proprietary trading income at 20%, financing income (17%), distribution income (7%) and others at 3%.

Within the lending segment under company’s wholly owned subsidiary Moneywise Financial Services, the loan book remains fairly well diversified across products with SME working capital loans forming 32% of AUM as on Dec-20, SME LAP forming 22%, capital market financing constituting 18%, onward lending at 16%, asset financing at 6% and consumer durable financing comprising remaining 5%. Further, incrementally the focus of Moneywise would be on lower ticket size loans and thereby increasing the granularity of the book.

Adequate Risk Management systems

SMC has well documented risk management framework to handle the risk in the broking, proprietary trading and lending business. There is Risk Management Committee of the Board which is responsible for identifying the risk and setting up processes to mitigate the risk. SMC has separate risk management teams which constantly evaluate the various risk, viz. market risk, credit risk, operational risk, and puts necessary mitigation measures in place on near real time basis for both broking and arbitrage operations. SMC has further tightened its risk management practice by implementing a system for automatic square-off of positions at day end, thereby further reducing the manual intervention risks. On the back of adequate risk management systems, the company has been able to control credit losses / write-offs in broking and lending segment with provisions and write-offs being 0.61% of the average total assets during FY20 and 0.88% (annualized) during 9M FY21.

Comfortable capital structure

The capital structure of SMC Group was comfortable overall gearing of SMC consolidated being 0.40x as on March-20 given the CARE adjusted tangible networth of Rs.641 crore and on-book debt of Rs.258 crore as on March 31, 2020. The overall gearing decreased from 1.19 times as on March-19 owing to decrease in on-book debt of the group. For nine months ending December 31, 2020, the company's consolidated overall gearing stood at 0.38 times. Besides the on-book debt, SMC also avails bank guarantees for trading on the exchanges. Bank Guarantees (at consolidated level) to the exchange stood at Rs.623 crore as on March 31, 2020. Since the majority of Moneywise's book remains equity funded, its capital structure remains comfortable with overall CRAR and Tier-I CRAR of 61.55% and 61.18% respectively as on Sep 30, 2020 and overall gearing at 0.52x as on Sep-20. End December 31, 2020, the gearing of Moneywise stood at 0.91 times

Key Rating Weaknesses

Dependency on capital markets which has inherent volatility

Capital market led activities which include broking, arbitrage operations, margin lending, portfolio management and depository services contribute about 53% share in SMC's consolidated revenue. The revenue from capital markets remains susceptible to market volatility, which exposes the company to the risk of volatility in income and profitability. Also, income earned as delayed payment charges / margin trade funding (MTF) tends to be volatile as also seen in significant reduction during FY20 due to regulatory changes restricting the number of days for which MTF can be allowed. The group's arbitrage book also remains susceptible to capital market conditions, however, most trades are hedged and algo-based and there is established track record of consistent stable profits in arbitrage book.

However, the dependence on capital market has reduced over years with the increased focus of group towards distribution segment and lending business. The distribution income and income from lending business contributes about 7% and 17% respectively to the total income in 9M FY21.

The ability of the group to further diversify the income profile by increasing the share of lending / NBFC business, distribution of various financial products and other segments thereby reducing the reliance on capital markets would be crucial to its credit profile.

Moderation in profitability in FY20

The profitability profile of SMC (consolidated) moderated in FY20 with SMC reporting net profit of Rs.23.86 crore on a net income of Rs.547.61 crore in FY20 as against net profit of Rs.74.78 crore in FY19 on a net income of Rs.562.35 crore in FY19. The profitability was impacted on account of increase in operating expenses of the group and provisioning cost at the NBFC level and owing to increase in losses in real estate vertical. SMC (conso) reported Adjusted PBILDT and PAT margin of 22.69% and 4.36% respectively in FY20 as against 29.36% and 13.30% respectively in FY19. Also, the RoNW declined to 3.74% in FY20 from 12.33% in FY19.

Further, during 9M FY21, SMC on a consolidated basis reported PAT of Rs.67.71 crore on net income of Rs.427.63 crore during 9M FY21. The annualized RoNW stood at 13.32% during 9M FY21.

Low seasoning of lending book, though on an improving trend. Borrower concentration risk prevails

SMC Group commenced lending business in 2008, however, there has been a significant change in product mix during the last 2 years. Thus, the asset quality trend is evolving given the loan book is under second credit cycle for many loan products. Also, given a moderate book size, nearly 27% of the portfolio entails loans of ticket size more than Rs.5 crore. The Top 10 borrowers constituted 19% of the loan book as on Dec-20 improved from 27% of the loan book as on Dec-19) and hence the borrower concentration continues to be high, though declining trend is seen. However most of these are secured loans (secured by immovable property, liquid securities, receivable, etc). Also, the concentration is expected to reduce further with company's focus on retail loans as well as loan run-off. The ability of Moneywise to maintain asset quality in the existing segments and reduce the share of larger ticket size loans (ticket size > Rs.5 crore) lending segment would be crucial.

During 9M FY21, the absolute GNPA and NNPA reduced to Rs.13.08 crore and Rs.8.03 crore respectively as on Dec-20 from March-20 levels. The decline in absolute GNPA was mainly on account of write offs of Rs.7 crore in 9M FY21 (from the loans which were 50% provided for). With the decline in absolute GNPA coupled with increase in loan book, the GNPA and NNPA ratio improved to 2.06% and 1.27% respectively as on Dec-20 from 4.22% and 2.45% respectively as on March-20. However, the proforma GNPA of Moneywise stood at 6% as on Dec-20.

Liquidity: Strong

The liquidity profile of SMC is strong supported by arbitrage book of Rs.115 crore which can be liquidated in case of need, comfortable capital structure and healthy level of margin utilization with exchanges. The company had free cash and bank balances of Rs.59 crore as on Dec-20. Furthermore, the company maintains adequate margin with stock exchanges (Average utilization of 60% over the period Apr-19 to June-20) and the unutilized margin offers liquidity cushion to SMC in the case of eventuality. The liquidity profile of Moneywise also remains adequate owing to largely capital funded loan book and support from group in terms of inter-corporate loans.

Analytical approach: CARE has based its assessment on the combined view of SMC Global Securities Limited including all its subsidiaries based on consolidated financials of SMC Global Securities Limited.

Applicable Criteria

Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Financial Ratios – Financial Sector
Rating Methodology: Consolidation
Criteria for Short Term Instruments
Rating Methodology – Non Banking Finance Companies (NBFCs)

About the Company

SMC Global Securities Limited (SMC), a Delhi based stock Broking Company which was incorporated on December 19, 1994 and is the flagship company of the SMC group. The group is one of the old integrated capital market intermediaries in the financial sector engaged in the business of broking, arbitrage trading, financial product distribution (Mutual Funds, Debt Products and Insurance), depository services, portfolio management services (PMS) and lending operations. SMC has pan-India branch and franchisee presence and is present in over 550 Cities and has a network of over 95 branches, 3,450+ employees, 2500+ Sub-brokers, 13,700+ Independent Distributors, client base: 18+ Lac as on Dec-20. AUM of Moneywise (NBFC) stood at Rs.644 crore as on Dec-20.

Brief Financials (Rs. Crore)	FY19(A)	FY20 (A)
SMC (Consolidated)	INDAS	IND AS
Total income	759.47	784.13
Net Income (adjusted for commission to sub-brokers)	562.35	547.61
Interest coverage (times)	2.63	2.07
Overall Gearing	1.19	0.40
Total Assets	2,301.96	1,832.96
RONW (%)	12.33	3.74
Moneywise (Standalone)		
NNPA (%)	1.70	2.46

A: Audited

#Note: Total Assets is calculated after excluding intangible assets and deferred tax assets

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating History for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: *Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3*

Complexity level of various instruments rated for this company: Annexure 4

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Commercial Paper Issue (Proposed)	-	-	-	25.00	CARE A1+

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Commercial Paper-Commercial Paper (Standalone)	ST	25.00	CARE A1+	-	1)CARE A1+ (02-Mar-20)	1)CARE A1+ (03-Sep-18)	-

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: NA

Annexure 4: Complexity level of various instruments rated for this company

Sr. No.	Name of the Instrument	Complexity Level
1.	Commercial Paper-Commercial Paper (Standalone)	Simple

Annexure 5: List of subsidiaries getting consolidated at SMC level as on March 31, 2020

S.No.	Company Name	Shareholding of SMC Global
	Indian Subsidiaries	
1	Moneywise Financial Services Pvt Ltd	100.00%
2	SMC Comtrade Limited	100.00%
3	SMC Capitals Limited	100.00%
4	SMC Investments & Advisors Limited	100.00%
5	Moneywise Finvest Limited	100.00%
6	SMC Insurance Brokers Pvt Limited	97.58%
7	SMC Global IFSC Pvt Limited	100.00%
8	SMC Real Estate Advisors Pvt Limited	100.00%
	Foreign Subsidiaries	
9	SMC Comex International DMCC	100.00%
1(	SMC Global USA Inc.	50.00%
	Joint Ventures	
1:	SMC and IM Capital Investment Manager LLP	50.00%

***** JV of SMC Investments & Advisors Limited which holds 50% stake in the company

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

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