August 05, 2022

Motilal Oswal Financial Services Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial Papers	2,500	2,500	[ICRA]A1+; reaffirmed
Long-term Principal Protected Market Linked Debentures	100	100	PP-MLD[ICRA]AA (Stable); reaffirmed
Non-convertible Debentures	300	300	[ICRA]AA (Stable); reaffirmed
Long-term Fund-based/ Non-fund Based Bank Lines	300	300	[ICRA]AA (Stable); reaffirmed
Total	**3,200**	**3,200**	

**Instrument details are provided in Annexure-I*

Rationale

To arrive at the ratings, ICRA has taken a consolidated view of the credit profiles of Motilal Oswal Financial Services Limited (MOFSL or Group), and its subsidiaries, including Motilal Oswal Wealth Limited (MOWL), Motilal Oswal Finvest Limited (MOFL) and Motilal Oswal Home Finance Limited (MOHFL), as the companies have operational and business synergies in addition to a shared name and management oversight.

The ratings take into account the Group's healthy operational profile, given its long-standing track record and established position in capital market related businesses with a focus on scaling up the annuity-based businesses. The ratings also consider MOFSL's healthy financial profile, with a steady performance in the capital market and allied businesses, and the healthy capitalisation profile on a consolidated basis. MOFSL reported a healthy profitability in FY2022 with a return on net worth of 25.7%, profit after tax (PAT)/net operating income (NOI) of 49.8% and the highest-ever PAT of Rs. 1,310.7 crore, supported by the strong performance across businesses as well as the mark-to-market (MTM) gains during the year. On the back of strong accruals, the gearing at the consolidated level improved to 1.08 times as of March 31, 2022 (1.14 times as of June 30, 2022) from 1.27 times as of March 31, 2021.

The aforesaid strengths are, however, partially offset by the inherently volatile nature of income from the capital market related business, though, the presence of the annuity-based income stream, which accounts ~50% of the Group's NOI provides some stability. In this regard, ICRA has taken cognisance of the moderation in MOFSL's performance in Q1 FY2023 as the geopolitical tensions and the adverse macroeconomic outlook dampened investor sentiments and the capital markets during the quarter.

The ratings also factor in the Group's relatively limited experience in the lending business with asset quality issues faced in the housing finance business (housed under MOHFL) in the recent past. It is noted that the Group undertook several remedial measures and extended greater managerial support with increased oversight and infused capital in the housing finance company (HFC), thereby underscoring its commitment to the venture. Also, while MOHFL reported fresh slippages in FY2021 and FY2022 on account of the Covid-19 pandemic induced stress, increased focus on collections coupled with the sale of stressed exposures to an asset reconstruction company (ARC; Rs. 122 crore in FY2022 and Rs. 114 crore in FY2021) helped the Group contain the reported asset quality indicators. The gross non-performing assets (GNPAs) stood at 1.6% (previous year (PY): 2.2%) and the net non-performing assets (NNPAs) stood at 0.9% (PY: 1.5%) as of March 31, 2022. ICRA notes that the asset quality moderated in Q1 FY2023 with GNPA of 2.2% and NNPA of 1.3%. Nonetheless, the new loans originated post the strengthening of the systems and processes since April 2018 have fared relatively well in terms of the asset quality with the adjusted 2-year lagged GNPA of 1.4% as of March 31, 2022; however, the book remains modest and is yet to be seasoned.

Going forward, the Group's ability to profitably scaleup the home finance business while maintaining healthy asset quality would remain critical from a credit perspective. Nevertheless, ICRA draws comfort from the sizeable accruals from the established capital market related business and the healthy capitalisation profile, which provide adequate buffer to absorb losses and incremental credit costs over the near term, if any. The Stable outlook reflects ICRA's expectation that MOFSL would maintain its credit profile supported by the performance of its capital market related business.

Key rating drivers and their description

Credit strengths

Established position and demonstrated track record in capital market related businesses – The Group has a presence in diverse business segments comprising retail and institutional broking, wealth management, margin funding, commodity broking, investment banking, asset management, private equity and housing finance. MOFSL serves as the main holding company and primarily houses the capital market business of the Group. MOFSL is an established player in the equity broking business with a track record of over three decades, and an aggregate adjusted[1] market share of 2.4% of the turnover in FY2022 (2.7% in FY2021 and 2.4% in FY2020).

While the Group caters to both retail and institutional clientele segments, the retail segment contributes ~87% to the gross broking income. The Group has scaled up its operations significantly over the years. It continues to be among the top 10 brokers in terms of active NSE clients, catering to 28.5 lakh customers through 98 branches and 6,895 franchises as of March 31, 2022, up from 19.7 lakh customers through 93 branches and 5,389 franchises as of March 31, 2021.

Healthy capitalisation profile– Supported by the strong internal capital generation trajectory, MOFSL's capitalisation level remains healthy with a consolidated net worth of Rs. 5,674.4 crore as on March 31, 2022 (Rs. 4,461.4 crore as on March 31, 2021 and Rs. 3,086.3 crore as on March 31, 2020). Although the Group's overall borrowings continued to increase due to the growth in the capital market loan book and other working capital requirements in the broking operations, the strong accruals across businesses supported an improvement in the consolidated gearing to 1.08 times (ex-MOHFL: 0.62 times) as on March 31, 2022 from 1.27 times as on March 31, 2021 and 1.48 times as on March 31, 2020. As of June 30, 2022 the Group's consolidated gearing was 1.14 times (ex-MOHFL: 0.67 times). ICRA notes that MOFSL's investments in listed equities, equity mutual funds, schemes of portfolio management service, private equity funds, real estate funds, and alternative investment funds (AIFs) form a sizeable proportion of the consolidated net worth. Nonetheless, the adjusted free net worth and gearing also remain comfortable.

Track record of healthy profitability – MOFSL's capital market business has achieved a significant growth in recent years. Additionally, supported by the improvement in the annuity-based fee income, the Group's NOI increased by 42% on a year-on-year basis to Rs. 2,633.8 crore in FY2022, following the 19% growth reported in FY2021. With the improvement in the scale of operations, MOFSL's consolidated net profit has more than quadrupled over the past three years. It reported an all-time high net profit of Rs. 1,310.7 crore (Rs. 1,312.5 crore, including share of joint ventures and associates) in FY2022, up from Rs. 1,203.0 crore in FY2021 and Rs. 215.4 crore in FY2020. ICRA notes that the improvement in the net profit was also boosted by MTM gains of Rs. 496.0 crore (PY: Rs. 859.9 crore) from the fund-based business.

Overall, MOFSL reported a healthy profitability in FY2022 with a consolidated return on net worth of 25.7% and PAT/NOI of 49.8% (five-year average return on equity (RoE) and PAT/NOI of 20.0% and 35.9%, respectively). In Q1 FY2023, the Group reported a decline in the net profit to Rs. 31.3 crore compared to Rs. 299.8 crore in Q4 FY2022, on account of the MTM losses due to the correction in the equity markets during this period. However, the operating profits continued to be healthy at Rs. 181.7 crore (Rs. 261.9 crore in Q4 FY2022).

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[1] *Excluding industry proprietary turnover*

Credit challenges

Exposed to volatility inherent in capital markets; however, presence of annuity-based businesses imparts some stability to Group's earnings profile – With the Group's focus on scaling up the annuity-based businesses such as asset and wealth management, and home finance, the annuity-based fee {typically booked as a percentage of the assets under management (AUM)} increased by a compound annual growth rate (CAGR) of 9% during the past three years to Rs. 1,322.1[2] crore in FY2022, up 34% YOY. The share of income from the Group's traditional lines of business (broking, capital market related lending, and investment banking) remains exposed to the volatility inherent in capital markets, as corroborated by the two instances of a decline in the revenue from these segments in the past nine years. ICRA notes that with the significant scale-up of the broking and allied income in recent years on the back of favourable market conditions, the share of income from the traditional business has increased to 50% of the NOI in FY2022 from 37% in FY2020 and the four-year average of 42%.

Also, it is noted that the Group has deployed sizeable capital as investments in mutual funds, portfolio management services (PMS), private equity (PE)/ real estate (RE) funds, AIFs, and strategic equity investments which exposes its profitability and net worth to the volatility in capital markets. Going forward, a material scaleup of the annuity-based business would be critical for the overall stability of the Group's earnings profile.

Relatively limited experience in lending business; however, performance of new originations so far provides some comfort – The Group's housing finance business, which commenced under Motilal Oswal Home Finance Limited (MOHFL) in May 2014, witnessed a deterioration in the asset quality in FY2018 and FY2019. The Group undertook several remedial measures, including the strengthening of the processes and systems, managerial support, increased supervision and capital infusion, to support the venture. Supported by these endeavors and the divestment of NPAs to an ARC, the Group was able to curtail the reported GNPA at 1.80% of advances as of March 2020 compared to 9.20% as of March 2019. However, with Covid-19 induced stress, the segment reported fresh slippages again during the past two years.

Given the focus on collections and the sale of stressed exposures to the ARC (Rs. 122 crore in FY2022 and Rs. 114 crore in FY2021), the Group managed to contain the reported asset quality indicators with GNPA of 1.6% (PY: 2.2%) and NNPA of 0.9% (PY: 1.5%) as of March 31, 2022. However, the standard restructured book was material at 8.8% of the overall book as of March 31, 2022. Further, in Q1 FY2023, the asset quality moderated further with GNPA of 2.2% and NNPA of 1.3% as of June 30, 2022. ICRA notes that the new loans originated post the strengthening of the systems and processes since April 2018 have fared relatively well in terms of the asset quality with adjusted 2-year lagged GNPA of 1.4%; though the book remains modest and is yet to be seasoned. Further, in the past few years, while the Group has forayed into newer geographies to improve its presence, the home loan book continues to be characterised by geographical concentration with the top 3 states accounting for 82% of the loan book, despite improving from 88% as of March 31, 2020.

In addition to housing finance, the Group has scaled up the capital markets-based loan book[3], which stood at ~Rs. 1,529 crore as of March 31, 2022 (~Rs. 1,058 crore as of March 2021). ICRA takes note of the market and credit risks associated with the capital market loan book, although the company's monitoring systems and hitherto healthy performance in this business provide comfort. The performance of the capital market and allied businesses, coupled with the healthy capitalisation profile, provides adequate buffer to absorb losses and incremental credit costs over the near term, if any.

Intense competition in capital markets – With increasing competition in equity broking and the advent of discount brokerage houses, the Group's market share of NSE active clients declined to 2.4% as of June 30, 2022 from 3.9% as on March 31, 2019. With the competitive intensity in this cyclical industry expected to remain high, pressure on profitability cannot be ruled out, especially during downturns. Nonetheless, the lower level of equity market penetration in the country offers significant untapped potential for growth.

2 Including dividend income from alternatives

[3] Includes margin funding/loan against shares

Liquidity position: Strong

MOFSL has a comfortable liquidity position at the consolidated level with free un-encumbered cash and bank balances of ~Rs. 700 crore, liquid investments of ~Rs. 1,200 crore and drawable but un-utilised lines of ~Rs. 1,300 crore as on June 30, 2022. These, along with collections from home loans and the short-term nature of capital market loans are adequate for covering the repayment obligations of ~Rs. 3,960 crore till March 31, 2023. The Group also has adequate liquidity for placing additional margin at the exchanges, if required. Furthermore, ICRA notes that the Group's investment book of ~Rs. 3,756 crore as on March 31, 2022, with investments in mutual funds, private equity, real estate funds and AIFs, non-convertible debentures and equity instruments, aids financial flexibility.

Rating sensitivities

Positive factors – ICRA could upgrade the ratings on a substantial and sustained improvement in the Group's profitability along with a diversification in the earnings profile, while maintaining healthy asset quality indicators and robust capitalisation.

Negative factors – The ratings could witness pressure if there is a significant deterioration in the asset quality in the lending business, thereby impacting the Group's profitability and capitalisation. Further, changes in the regulatory environment, which may adversely impact the company's business operations and financial performance, would be a key rating sensitivity.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Rating Methodology for Entities in the Broking Industry Consolidation and Rating Approach Rating Methodology for Non-banking Finance Companies
Parent/Group support	Not Applicable
Consolidation/ Standalone	ICRA has taken a consolidated view of MOFSL along with its subsidiaries, which are engaged in various activities such as equity broking and distribution, commodity broking, margin funding, institutional equities, asset, wealth and portfolio management services, private equity, investment banking and housing finance

About the company

Incorporated in 2005, MOFSL serves as the holding company of the Motilal Oswal Group, which is among India's leading providers of capital market related services. The company, through its subsidiaries, provides broking and distribution services, asset, wealth and portfolio management services, private equity and housing finance.

MOFSL reported a consolidated net profit of Rs. 1,310.7 crore on NOI of Rs. 2,633.8 crore in FY2022 compared to Rs. 1,203.0 crore and Rs. 1,851.1 crore, respectively in FY2021. At the consolidated level, the Group's net worth stood at Rs. 5,674.4 crore as on March 31, 2022.

Key financial indicators

MOFSL (standalone)	FY2020	FY2021	FY2022
Brokerage income	435.4	674.3	845.0
Net interest income	146.2	158.9	262.0
Other non-interest income	43.7	57.7	165.9
Net operating income (NOI)	228.7	121.9	172.7
Total operating expenses	854.0	1,012.8	1,445.6
Profit before tax	194.1	876.3	864.1
Profit after tax (PAT)	196.8	750.7	706.8
Net worth	2,764.1	3,616.6	4,242.1

MOFSL (standalone)	FY2020	FY2021	FY2022
Borrowings	1,429.7	2,079.1	2,170.9
Gearing (times)	0.52	0.57	0.51
Cost-to-income ratio	57.0%	59.8%	57.1%
Return on net worth	7.3%	23.5%	18.0%
PAT/NOI	23.0%	74.1%	48.9%

Source: *Company, ICRA Research; All ratios as per ICRA's calculations*

Key financial indicators

MOFSL (consolidated)	FY2020	FY2021	FY2022
Brokerage income	447.3	695.9	869.7
Fee income (other than broking)	789.5	764.6	1,025.9
Net interest income	273.4	323.7	557.3
Other non-interest income	47.0	66.9	180.9
Net operating income (NOI)	1,557.2	1,851.1	2,633.8
Total operating expenses	962.6	1,070.6	1,419.3
Profit before tax	285.2	1,458.4	1,615.8
Profit after tax (PAT)	215.4	1,203.0	1,310.7
Profit after tax including associate & joint venture	189.6	1,264.7	1,312.5
Net worth	3,086.3	4,461.4	5,674.4
Borrowings	4,636.3	5,693.6	6,154.0
Gearing (times)	1.48	1.27	1.08
Cost-to-income ratio	61.8%	57.8%	53.9%
Return on net worth	6.9%	31.6%	25.7%
PAT/NOI	13.8%	65.0%	49.8%

Source: *Company, ICRA Research; All ratios as per ICRA's 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 (FY2023)					Chronology of Rating History for the Past 3 Years				
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of March 31, 2022 (Rs. crore)	Date & Rating in FY2023		Date & Rating in FY2022				Date & Rating in FY2021
					Aug 05, 2022	Apr 29, 2022	Feb 24, 2022	Nov-02, 2022	Sep 20, 2021	Aug 09, 2021	Dec 16, 2020 Aug 07, 2020
1	**Commercial Papers**	Short Term	1,500	450	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-	-	-	-
2	**Commercial Papers**	Short Term	1,000	1,000	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-	-	-
3	**Long-term Principal Protected Market Linked Debentures**	Long Term	100	78	PP-MLD [ICRA]AA (Stable)	PP-MLD [ICRA]AA (Stable)	PP-MLD [ICRA]AA (Stable)	PP-MLD [ICRA]AA (Stable)	PP-MLD [ICRA]AA (Stable)	-	-
4	**Non-convertible Debentures**	Long Term	300	300	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
5	**Bank Lines – Unallocated**	Long Term	-	-	-	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	-
6	**Long-term Fund-based/ Non-fund Based Bank Lines**	Long Term	300	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	-	-	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Commercial Papers	Very Simple
Long-term Principal Protected Market Linked Debentures	Moderately Complex
Non-convertible Debentures	Very Simple
Bank Lines	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: www.icra.in

Annexure-I: Instrument details

ISIN/Banker Name	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
INE338I07057	Non-convertible Debentures	Nov 06, 2020	7.60%	FY2024	195.00	[ICRA]AA (Stable)
INE338I07065	Non-convertible Debentures	Feb 05, 2021	7.25%	FY2024	105.00	[ICRA]AA (Stable)
INE338I07073	Long-term Principal Protected Market Linked Debentures	Sep 22, 2021	NIFTY50 Index Linked	FY2024	100.00	PP-MLD[ICRA]AA (Stable)
INE338I14DH1	Commercial Papers	May 04, 2022	5.40%	Aug 03,2022	150.00	[ICRA]A1+
INE338I14DJ7	Commercial Papers	May 25, 2022	6.30%	Sep 09, 2022	150.00	[ICRA]A1+
INE338I14DL3	Commercial Papers	Jun 15, 2022	6.15%	Sep 14, 2022	200.00	[ICRA]A1+
INE338I14DM1	Commercial Papers	Jul 21, 2022	6.80%	Dec 15, 2022	100.00	[ICRA]A1+
NA	Commercial Papers – Yet to be Issued	NA	NA	NA	1,900.00	[ICRA]A1+
NA	Long-term Fund-based/ Non-fund Based Bank Lines	Feb 21, 2022	NA	FY2024	300.00	[ICRA]AA (Stable)

Source: *Company*

Annexure-II: List of entities considered for consolidated analysis

Company Name	MOFSL Ownership (%)	Consolidation Approach
Motilal Oswal Commodities Broker Private Limited	100.00	Full Consolidation
Motilal Oswal Investment Advisors Limited	100.00	
MO Alternate Investment Advisors Private Limited	100.00	
Motilal Oswal Finvest Limited	100.00	
Motilal Oswal Wealth Management Limited	100.00	
Motilal Oswal Asset Management Company Limited	100.00	
Motilal Oswal Trustee Company Limited	100.00	
Motilal Oswal Securities International Private Limited	100.00	
Motilal Oswal Capital Markets (Singapore) Pte. Limited.	100.00	
Motilal Oswal Capital Markets (Hong Kong) Private Limited	100.00	
Motilal Oswal Home Finance Limited	97.71	
Motilal Oswal Finsec IFSC Limited	100.00	
Glide Tech Investment Advisory Private Limited	100.00	
TM Investment Technologies Pvt. Ltd	63.83	
India Business Excellence Management Company	100.00	
Motilal Oswal Asset Management (Mauritius) Limited	100.00	
Motilal Oswal Capital Limited	100.00	
India Reality Excellence Fund II LLP	20.44	

Source: *MOFSL annual report FY2022;* ***Note:*** *ICRA has taken a consolidated view of the parent (MOFSL), its subsidiaries and associates while assigning the ratings*

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