

## IIFL Capital Services Ltd — Aug 2022 Quarterly Analysis

### 1. VERDICT & BUSINESS QUALITY SNAPSHOT

*The punchline. Read this first — it frames everything below.*

**Result:** Weak Miss **One-line:** Profitability collapsed by 37% YoY as a rigid, high-fixed-cost structure (tech/employees) met a cooling market and sharply lower Investment Banking realizations.

Dimension	This Quarter	Signal / Evidence	Sentiment
Beat/Miss vs Guidance / Prior Quarter	Weak Miss	PAT down 45% QoQ; PBT margins compressed from 32% to 20% YoY.	☐
Earnings Quality	Low (One-off/Accounting driven)	Impacted by MTM losses on BSE shares and ₹18.68 Cr finance cost spike.	☐
Guidance Confidence	Weak	Mgmt admit inability to "dramatically" cut costs despite revenue softening.	☐
Management Credibility	Neutral	Transparent about cost pressures but failed to anticipate margin deleverage.	☐
Business Quality Signal	Deteriorating	Cash market share fell (2.9% to 2.6%); 90% of new clients on low-yield discount plans.	☐
Key Q&A Exchange	Q1 Margin Strategy	Mgmt admits headcount/tech costs are sticky long-term investments.	☐
The Street's Primary Anxiety	Operating Deleverage	Rising expenses (+29% YoY) vs sluggish top-line (+10% YoY).	☐
Capital Cycle Stage	Consolidation	High headcount growth (2,136 to 2,500) now being digested.	☐
Margin / Return Ratio Trajectory	Deteriorating	PBT Margin: 20.8% (Current) vs 32.3% (YoY).	☐
Pricing Power	Eroding	90% of new acquisitions are opting for flat/discount brokerage.	☐
FCF Conversion & Quality	Not in document	CFO/PAT data not provided for this quarter.	☐
Competitive Moat Signals	Stable	Institutional strength remains, but retail being squeezed by discount brokers.	☐
Balance Sheet Strength	Adequate	Net worth stable at ₹1,230 Cr.	☐
Working Capital Efficiency	Deteriorating	Finance costs up 40% YoY to support margin trading book growth.	☐
Mgmt Guidance Track Record	Mixed	IB pipeline touted but dependent on volatile market conditions.	☐
Key Vulnerability / Red Flag	Cost Rigidity	Employee costs up 31% YoY while profitability is at a multi-quarter low.	☐
Management Tone	Cautious & Defensiveness	Defensive on high cost-base; cautious on market volatility.	☐

**Sentiment:** ☐Negative

**Key Takeaways: Positives:** \* Total market share marginally increased to 1.18% (from 1.15% QoQ). \* Investment Banking pipeline remains healthy with 7 DRHPs filed during the quarter. \* Distribution income, while down YoY, remains a key cross-sell engine (₹40 Cr).

**Negatives:** \* **Operating Deleverage:** Total expenses grew 29% YoY, nearly triple the revenue growth rate of 10%. \* **Segment Fatigue:** Investment Banking income fell 55% QoQ (from ₹66 Cr to ₹30 Cr) as IPO activity cooled. \* **Market Share Loss:** Cash segment market share dropped from 2.9% to 2.6%, reflecting institutional segment pressure. \* **Sticky Costs:** Management admitted that headcount (up 17% YoY) and technology investments cannot be easily curtailed, suggesting continued margin pressure if volumes don't recover.

## 2. BUSINESS PERFORMANCE

### 2A. KEY METRICS

DATA SOURCE: PPT figures used as primary source. Concall used for Mgmt Commentary and granular segment data.

Metric	Current Qtr	YoY Change	QoQ Change	Trend	Mgmt Commentary
Total Income	₹294.8 Cr	↑ 10%	↓ 19%	↓	Driven by 12% brokerage growth; offset by distribution fall.
PAT	₹40.3 Cr	↓ 37%	↓ 45%	↓	Impacted by MTM losses on BSE shares and rising fixed costs.
Fee Income (IB)	₹29.0 Cr	↑ 26%	↓ 55%	↓	Sharply down QoQ as the record Q4 base was not repeatable.
Brokerage Income	₹145.0 Cr	↑ 12%	↓ 20%	↓	Softening retail sentiment and lower cash volumes.
Distribution Income	₹40.0 Cr	↓ 17%	↓ 28%	↓	High base last year due to NCD public issues; Q4 seasonal peak.
Finance Cost	₹18.68 Cr	↑ 40%	↑ 2%	↓	Increased borrowing to fund growth in the MTF (Margin Trading) book.
Employee Cost	₹77.5 Cr	↑ 31%	↓ 10%	↓	Headcount increased to 2,500 from 2,136; variable pay impact.
AUM (under advisory)	₹1,12,000 Cr	↓ (est)	↓ (est)	↓	Decline primarily due to negative Mark-to-Market (MTM) market movement.
Cash Market Share	2.6%	Not in doc	↓ 30 bps	↓	Loss attributed to the institutional segment performance.
Total Market Share	1.18%	Not in doc	↑ 3 bps	→	Marginal gain on back of F&O volumes.

### 2B. SEGMENT BREAKDOWN

Segment	Revenue (₹ Cr)	YoY Growth	Margin (%)	Trend	vs Company Avg	Key Development
Retail Brokerage	₹145.0*	↑ 12%	Not stated	↓	In-line	90% of new clients opting for flat/discount plans.
Investment Banking	₹29.0	↑ 28%	High	↓	Above Avg	3 transactions completed; 7 DRHPs filed; healthy pipeline.
Distribution	₹40.0	↓ 17%	Not stated	↓	In-line	Decline due to lack of large NCD issues vs last year.
Institutional Brok.	Not stated	Not stated	Not stated	↓	Below Avg	Identified as the cause for cash market share loss.

\*Note: Brokerage income includes both retail and institutional.

### 3. MANAGEMENT OUTLOOK & EXECUTION TRACKER

Dimension	Category	Management Target / Claim	Required Run-Rate / Mathematical Feasibility	Historical Delivery (Did they do what they promised last Q?)	Risk Flag
Guidance	Margins	Expected improvement in coming quarters.	Requires ~₹20 Cr cost reduction or ₹50 Cr+ revenue jump to hit 30% PBT.	Missed (Margins fell from 32% to 20% YoY).	<b>High</b> - Costs are "sticky."
Guidance	IB Pipeline	7 DRHPs filed; healthy advisory pipeline.	Dependent on market volatility/secondary market stability.	Delivered (3 deals closed in a tough Q1).	<b>Medium</b> - Timing risk.
Strategy	Customer Acquisition	Optimize Cost of Acquisition; 60-70% DIY.	Needs higher cross-sell as 90% are on low-yield brokerage.	First entry.	<b>Medium</b> - Low ARPU clients.
Strategy	Technology	Tech is the key differentiator for experience.	Sustained admin/tech spend (₹5.9 Cr) required.	Ongoing investment.	<b>Low</b> - Non-negotiable spend.
Macro	Inflation/Rates	Volatility likely to remain throughout the year.	N/A	Correctly anticipated market choppiness.	<b>Low</b> - Macro reality.
Balance	MTF Growth	Borrowing increased to fund MTF book.	Interest income must exceed 10%+ cost of funds.	Ongoing growth.	<b>Medium</b> - Spread risk.

## 4. ANALYST Q&A

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Q#	Relevance (1-5)	Analyst / Firm	Theme Cluster	Category	Underlying Concern	Management Response & Investment Implication	Evaded / Not Addressed	Credibility (1-5)	Verdict
1	5.0	Mudita Nahar / Abakkus AMC	Margin Sustainability	Financials	Why did margins shrink so much and what is the recovery plan?	Management attributed the squeeze to headcount increases and annual increments that were "generous" due to the prior bull year. This implies a structurally higher cost base that will drag on ROE until revenue cycles back up.	None	3.5	Deflected on timeline
2	4.0	Mudita Nahar / Abakkus AMC	Revenue Strategy	Management Commentary	Is there a specific strategy to boost the top line?	The focus remains on customer acquisition, cross-selling, and waiting for the investment banking pipeline to "consume" as market conditions improve. Success is highly beta-dependent on the broader market rather than internal levers.	Specific revenue targets	3.0	Vague
3	4.5	Kajal / ICICI Securities	Market Share	Business Overview	Did the company gain market share in the cash segment?	Management admitted a marginal decline in cash market share to 2.6% (from 2.9%) due to weakness in the institutional segment. This	Exact reasons for insti loss	4.0	Directional

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						signals competitive pressure or a shift in institutional flow away from the firm.			
4	4.0	Kajal / ICICI Securities	Customer Quality	Business Overview	What percentage of new customers are DIY vs assisted, and on which plans?	Approximately 60-70% are DIY, and 90% of new brokerage clients are opting for discount/flat plans. This confirms a pivot toward a high-volume, low-yield model that requires massive scale to offset the current fixed cost base.	None	4.0	Clear & quantified

#### PATTERN FLAGS & SENTIMENT

The primary anxiety among analysts was **Operating Deleverage**. Multiple questions focused on why expenses (especially employee and technology costs) were allowed to grow so rapidly (+29% YoY) right as the market slowed down. Management's posture was somewhat defensive, justifying the "generous" increments as a reward for the previous year's performance and framing current headcount as a long-term necessity. This concern was not fully resolved, as management admitted they cannot "dramatically" cut these costs, making the company's profitability highly vulnerable to any further market softening.

**Analyst Sentiment Verdict:** Analysts appeared skeptical of the current cost structure. The friction point was clearly the mismatch between a record headcount/tech spend and a double-digit decline in QoQ revenue. Credibility on margin management has deteriorated versus the high-performance narrative of FY22. The greatest risk remains the "sticky" nature of these costs in a low-growth environment.

## 5. WHAT CHANGED vs PRIOR QUARTER

*First entry — no prior quarter to compare.*

What Changed	Prior Quarter	This Quarter	Direction
Revenue (Total)	€362.1 Cr	€294.8 Cr	↓ 19%
PBT Margin	29.1% (Q4)	20.8% (Q1)	↓ 830 bps
IB Revenue	€66.0 Cr	€30.0 Cr	↓ 55%
Cash Market Share	2.9%	2.6%	↓ 30 bps
Employee Costs	€86.1 Cr (Q4)	€77.5 Cr	↓ 10% (Seasonal/Bonus)
Finance Costs	€18.3 Cr	€18.7 Cr	↑ 2%
Headcount	~2,300 (est)	2,500	↑

STOP HERE.