

Central Depository Services (India) Limited
(Subscribe)

Analyst:

Vaibhav Joshi

Rohit Rai

Kunal Sharma

16 June 2017

IPO details

| Key Data | |
|--------------------------------|---------------------------------|
| Issue Opens | 19-Jun-17 |
| Issue Closes | 21-Jun-17 |
| Equity Shares Offered (in mn.) | 35.16 |
| QIB | Up to 50% |
| NIB | Min 15% |
| Retail | Min 35% |
| Face Value (₹) | 10 |
| Price Band (₹) | 145-149 |
| Max. Issue Size (₹ mn) | 5,239 |
| Lot Size (Eq. Shares) | 100 shares and multiple thereof |

| Valuation | @ ₹145 per share | @ ₹149 per share |
|-------------------------|------------------|------------------|
| Market Cap (₹ mn) | 15,152 | 15,570 |
| Net Debt (₹ mn) | 0 | 0 |
| Enterprise Value (₹ mn) | 14,669 | 15,166 |
| EV/ Sales | 10.0 | 10.4 |
| EV/ EBIDTA | 12.2 | 12.6 |
| P/B | 2.8 | 2.9 |
| P/E | 17.5 | 18.0 |

Source: Red Herring Prospectus, Destimoney Research

| | Pre Issue | | Post Issue [^] | |
|----------------|-------------|-----------|-------------------------|-----------|
| | # mn Shares | % Holding | # mn Shares | % Holding |
| Promoters | 52.3 | 50.0% | 25.1 | 24.0% |
| Institutions | 52.2 | 50.0% | 44.3 | 42.3% |
| Offer For Sale | | | 35.2 | 33.7% |
| Total | 104.5 | 100.00% | 104.5 | 100.0% |

Promoters

Object of Issue

- To gain the listing benefits and for general corporate purposes
- Enhance it's visibility and brand image and provide liquidity to it's existing shareholders.

Recommendation

- The two player industry with lower penetration provides immense opportunities for CDSL and NSDL to co-exist and. CDSL management's focus on increasing retail participation from tier II and tier III cities, unique model producing recurring income and strong financial performance reinforces confidence in the company's future prospects.
- On valuation front, even though no listed peer exists, at the upper price of Rs. 149, the PE multiple of 18x and EV/EBITDA multiple of 12.6x it does not seem to be expensive considering the strong balance sheet and earnings and the healthy return ratios. Therefore, we recommend to **SUBSCRIBE** the issue at cut off price.

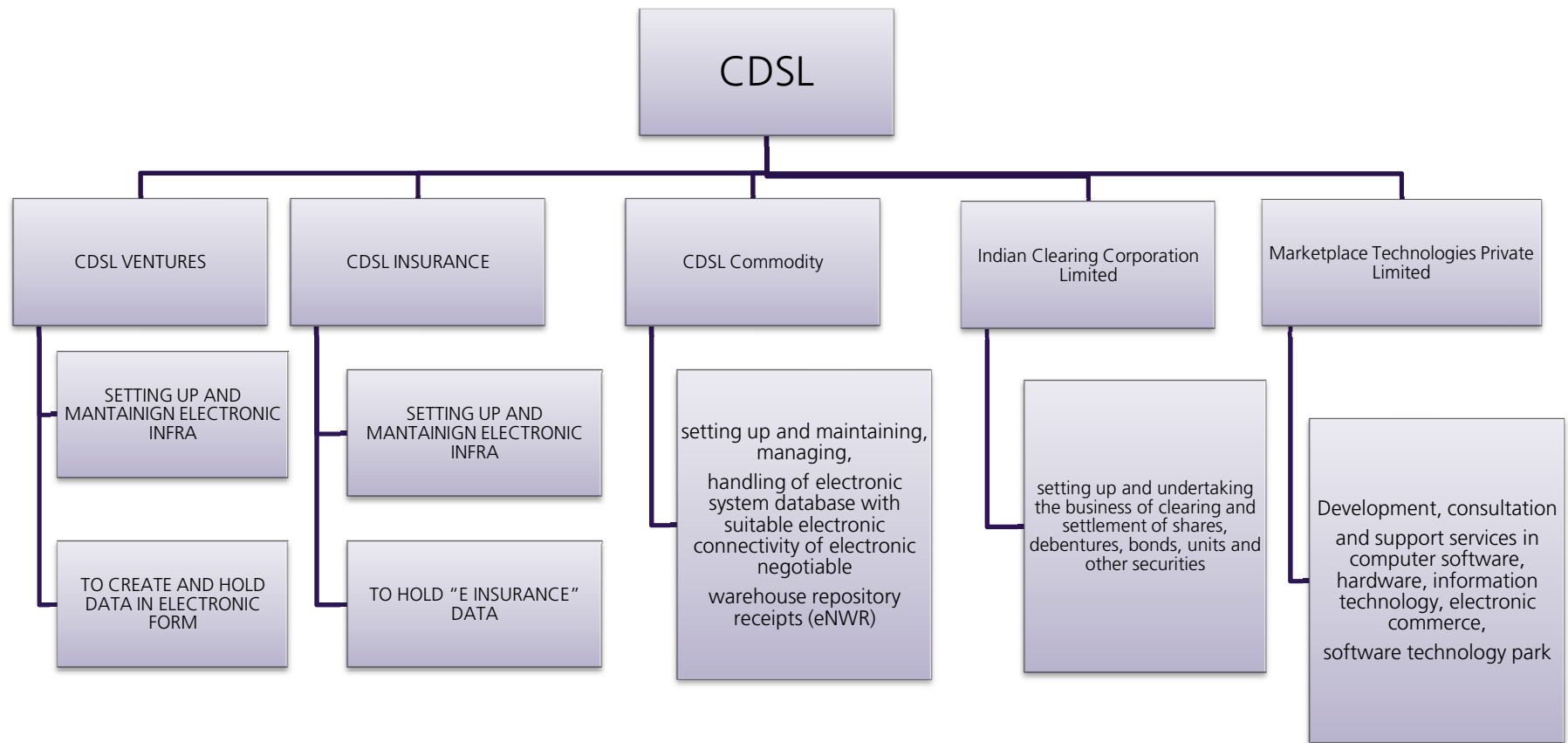
[^]NOTE: Valuation Parameters considered are fully subscribed issue for FY16 financials

Company Profile

- ❑ CDSL commenced its depository business in 1999 with the objective of providing convenient, dependable and secure depository services at affordable cost to all market participants. CDSL was initially promoted by the BSE which subsequently divested a part of its stake to leading Indian banks. CDSL has connectivity with clearing corporations of all the leading Indian stock exchanges including the BSE, National Stock Exchange ("NSE") and Metropolitan Stock Exchange of India. CDSL has also entered into MoUs with depositories globally including with DTCC, JASDEC and Euroclear.
- ❑ CDSL is the leading securities depository in India by incremental growth of Beneficial Owner ("BO") accounts over the last three Fiscals and by the total number of registered Depository Participants ("DPs"), as at the end of Fiscal 2016, according to the CRISIL Report. However, in terms of market share, CDSL is the second largest depository in India.
- ❑ Services Offered to the following clients: Depository Participants and other capital market intermediaries, Corporates, Capital market intermediaries, Insurance Companies, Others (such as online services such as e-voting, e-Locker, National Academy Depository)
- ❑ CDSL facilitates holding of securities in the electronic form and enables securities transactions to be processed by book entry. CDSL was set up with the objective of providing convenient, dependable and secure depository services at affordable cost to all market participants. The balances in the investors account recorded and maintained with CDSL can be obtained through the Depository participant (agents of the depository). The depository system has effectively eliminated paper-based certificates which were prone to be fake, forged, counterfeit resulting in bad deliveries. CDSL offers an efficient and instantaneous transfer of securities.
- ❑ CDSL was initially promoted by BSE Ltd. which has thereafter divested its stake to leading banks as "Sponsors" of CDSL. The sponsors include State Bank of India; Standard Chartered Bank; HDFC Bank Limited; Canara Bank; Bank of India; Bank of Baroda; Union Bank of India.
- ❑ All leading stock exchanges like the BSE Ltd, National Stock Exchange and Metropolitan Stock Exchange of India have established connectivity with CDSL. CDSL has , in recent times launched an array of facilities in an attempt to diversify. Such services include an "E-Locker" for securely storing documents , will generation and storage services and electronic KYC.

Source: Red Herring Prospectus, Destimoney Research

Corporate Structure



Source: Red Herring Prospectus, Destimoney Research

Historical Milestones

- 99 •The Union Finance Minister of India, Mr. Yashwant Sinha flagged off the operations of the company
- 99 •The first settlement of trades in demat mode through BOI Shareholding Limited, the clearing house of BSE, began.
- 02 •Company launched its internet facility “easi” (electronic access to securities information).
- 02 •inter-depository transfer commenced. This facility enables on-line transfer of securities between both the depositories any time during the specified business hours.
- 04 •Company launched its internet facility “easiest” (electronic access to securities information & execution of secured transaction).
- 06 •CDSL Ventures, a wholly owned subsidiary of theCompany was incorporated
- 07 •Company signed an MoU with the Depository Trust & Clearing Corporation of New York (“DTCC”), designed to build a closer working relationship and exchange of information.
- 08 •Number of active demat accounts with theCompany touched 4.5 million.
- 08 •Company signed an MoU with Japan Securities Depository Center, Inc. (“JASDEC”) of Tokyo, designed to build a cooperative relationship.
- 08 •Company signed an MoU with National Depository Center (“NDC”) to bolster economic relations between India and Russia by encouraging cooperation through the mutual exchange of experience
- 08 • Company signed an MoU with Taiwan Depository & Clearing Corporation (“TDCC”) aimed at mutual benefits and further development in the financial market by cooperation in operations and operation linkages, exchange of personnel and new developments
- 09 •Honourable Minister for Corporate Affairs of India, Mr. Salman Khurshid launched the Company’s e-voting platform
- 09 •the Company and Bursa Malaysia Depository Sdn. Bhd. (“Bursa Malaysia Depository”) signed an MoU to pursue cooperative relationship and opportunities in the areas of securities clearing and depository.
- 12 •Mr. U. K. Sinha, SEBI Chairman launched CDSL Ventures KRA, India’s first and largest KYC Registration agency
- 15 •The number of active demat accounts opened with the Company crossed 10 million.

Source: Red Herring Prospectus, Destimoney Research

Key Strengths and Future Strategies:

- ❑ **Stable revenue base and multiple offerings:** CDSL service offering spans across the segments including equity market, debt market, mutual fund and insurance. The diverse client base including DPs, corporates, stock exchanges, clearing corporations, registrars and the investors provides multiple streams of stable and recurring operating revenue. The fixed annual charges collected from registered companies and the transaction-based fees from DPs are the most reliable sources of revenue. The niche services like e-notices and e-voting add further to the revenue stream. As of April 30, 2017, CDSL had opened approximately 325,000 e-Insurance accounts, holding more than 66,000 insurance policies in electronic form.
- ❑ **Diversification of revenue streams:** In addition to the core services of electronic custody and trade settlement , CDSL also provides other services such as pledging, automatic delivery of securities to clearing corporations , distribution of cash and non cash benefits such as bonuses and rights on behalf of the companies.
- ❑ **High economies of scale:** The company has emerged as a leading securities depository in India by incremental growth of BO accounts according to the CRISIL Report. The peculiar nature of the business requiring largely fixed costs which include employee wages and post employee benefits and software development and maintenance costs creates a room to generate economies of scale with the increasing volume. The growth in BO accounts at CAGR of 12.98% over the last three fiscals has been reflecting in the margins achieving the economies of scale. During the period, the company’s total expenditure has remained almost constant reflecting in increased profitability and dividend payouts.

| | FY14 | FY15 | FY16 | FY17 |
|-------------------------|-----------|-----------|------------|------------|
| Live Companies | 8,630 | 9,399 | 10,021 | 9,694 |
| Depository Participants | 578 | 574 | 583 | 584 |
| DP Locations | 11,381 | 11,877 | 16,764 | 17,436 |
| BO Accounts | 8,777,049 | 9,610,002 | 10,790,738 | 11,692,031 |

- ❑ **Data sharing arrangements.** The company has MOUs with the Malaysian , Japanese , Russian, Taiwanese South Korean and Nepalese stock exchanges and depository agencies for exchange of information, collaboration and cooperation.

Source: Red Herring Prospectus, Destimoney Research

Key Strengths and Future Strategies:

- ❑ **Impressive growth in securities holding and retail participation:** The number of securities held by CDSL grew at a CAGR of 15% over FY 12-16. This rise has been possible due to an increase in non equity traded securities including bonds and other money market instruments which is set to continue. The account growth for CDSL has been especially high and this is set to boom over the years to come owing to a growth in per capita income. The retail participation is also set to boom due to the various investor assistance and education programs being launched.
- ❑ **Mutual Funds and Insurance segment driving the growth:** The **Indian mutual fund industry** has been a major contributor to the depositories' revenue. The net inflow from mutual funds have grown substantially from 2009 due to confidence in domestic markets and timely initiatives taken by SEBI. The insurance industry is set to ramp up its equity participation and an increase in equity activity by EPFO will also be beneficial to the depository as they all majorly deal in the cash segment.
- ❑ **Continue to develop DP relationships and networks:** The company aims at expanding its customer base and strengthen its already existing networks by introducing new products and services to ensure faster and easier processing of transaction and data. The focus is to strategically reach out to the underserved tier II and tier III cities which will help in further enhancing retail participation.
- ❑ **Competitive strategies on anvil with improving efficiency:** In order to remain competitive in the oligopoly market space, the company has the focus on providing quality services at attractive prices. Leveraging upon the economies of scale and the increasing operating efficiency are the keys to achieve the goal. The management has plans on anvil to improve the efficiency through-
 - Development of back office system to ensure standardization to reduce the risk of errors.
 - Offering single demat account which holds a wide variety of securities including fixed deposits.
 - Development of a centralised automated system to decrease time for processing.
 - Development of easier ways to opt for consolidated account statements (CAS)
- ❑ **Continue to invest in investor education to increase potential customers:** The company plans to increase financial inclusion by holding investor awareness camps to increase investor awareness and foster retail participation. The company also plans to focus on tier 2 and tier 3 cities to bring in the new client base across geographies, professions and age groups. CDSL conducted over 400 investor awareness programs in Fiscal 2016.

Source: Red Herring Prospectus, Destimoney Research

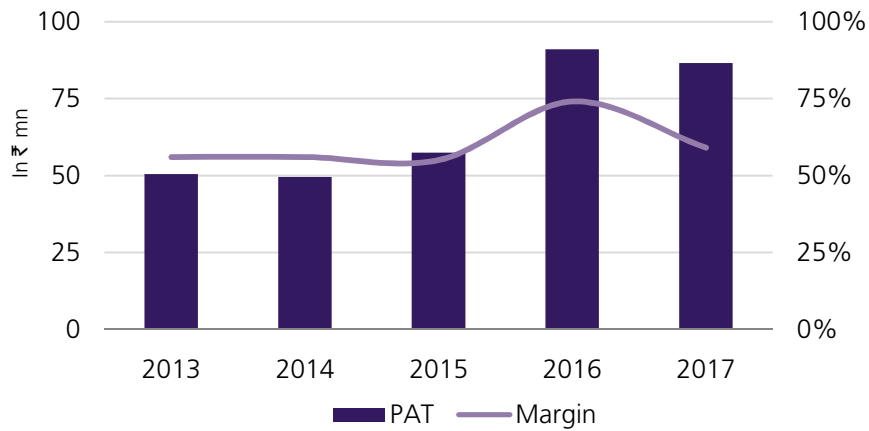
Strong Financials:

- ❑ The company has a healthy financial position. The revenue of the company has been growing at a CAGR of ~11% from FY13 -17. It's main source of revenue is transaction charges, account maintenance charges and settlement charges paid by depository participants and annual fees , corporate action charges and e voting charges paid by companies whose security are admitted in their systems.
- ❑ The company has a PAT growth of CAGR ~12% over the aforesaid period which stands at Rs 87 Cr as at march 2017. The company also has an EBITDA growth of CAGR ~20% over the same period.
- ❑ The depository segment has been witnessing a revenue growth of CAGR ~9.5% over the aforementioned period, standing at Rs 148Cr for the year ended March 16. The data processing segment has been witnessing a revenue growth of CAGR ~5.4% over the same period which stands at 29.6Cr. The ROCE for the depository and data processing segment stand at ~23% and ~26% respectively.
- ❑ As at march 17 the company had an EPS of Rs 6.49 per share which grew at CAGR ~8% over FY13-17.
- ❑ CDSL's revenue from operations includes transaction charges, account maintenance charges and settlement charges paid by DPs and annual fees, corporate action charges and e-voting charges paid by companies whose securities are admitted to its systems.
- ❑ As of April 30, 2017, CDSL had:
 - Over 12.4 million investor accounts. In Fiscal 2017, we held a 59% market share of incremental BO accounts with a net growth in BO accounts of 13.68% from Fiscal 2016 to Fiscal 2017.
 - Over 253 billion securities of 9,934 issuers under our custody representing a total value of `18.3 trillion.
 - 589 registered DPs who had over 17,000 service centers across India.
 - Over 15 million KYC records with a market share of approximately 67%.
- ❑ On a consolidated restated basis, CDSL's total revenue grew at a CAGR of 13.33% from ₹1,454.69 million in Fiscal 2015 (proforma) to ₹1,868.51 million in Fiscal 2017 and our net profit after tax grew as restated at a CAGR of 21.96% from ₹576.69 million in Fiscal 2015 (proforma) to ₹857.81 million in Fiscal 2017.

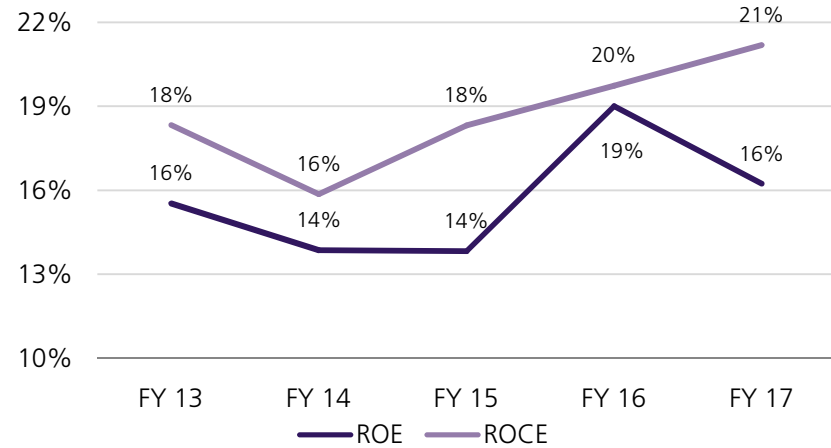
Source: Red Herring Prospectus

Improving financials

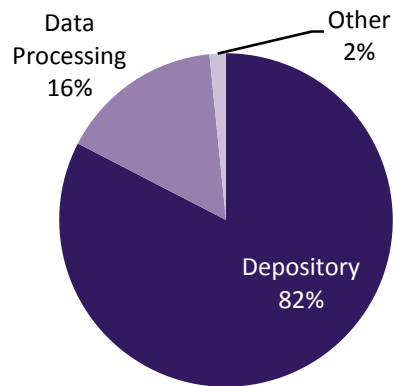
PAT and PAT margin



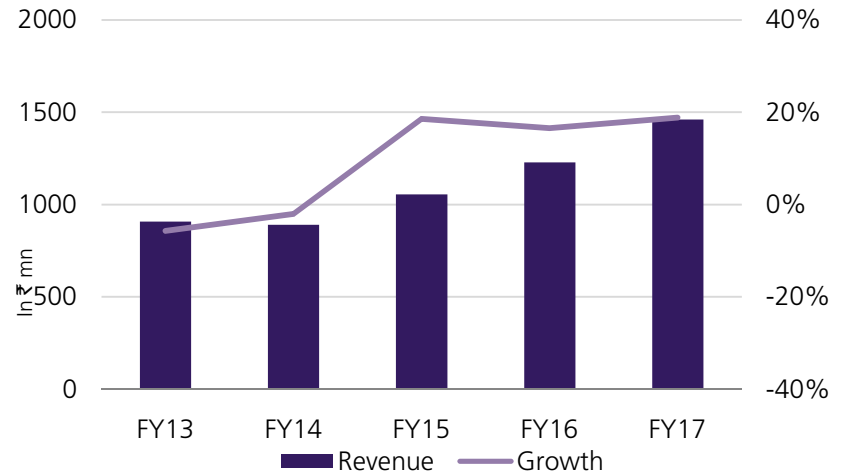
ROE and ROCE ratios



Sale composition



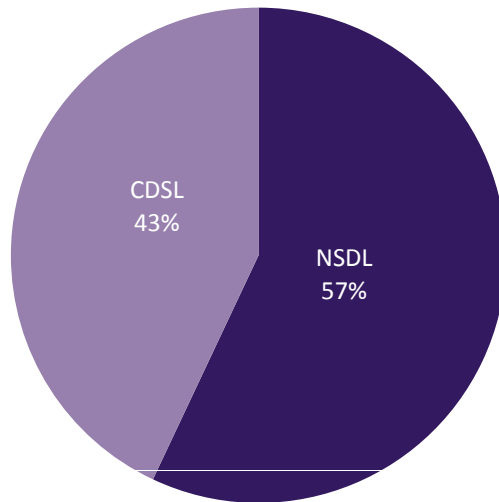
Revenue Growth



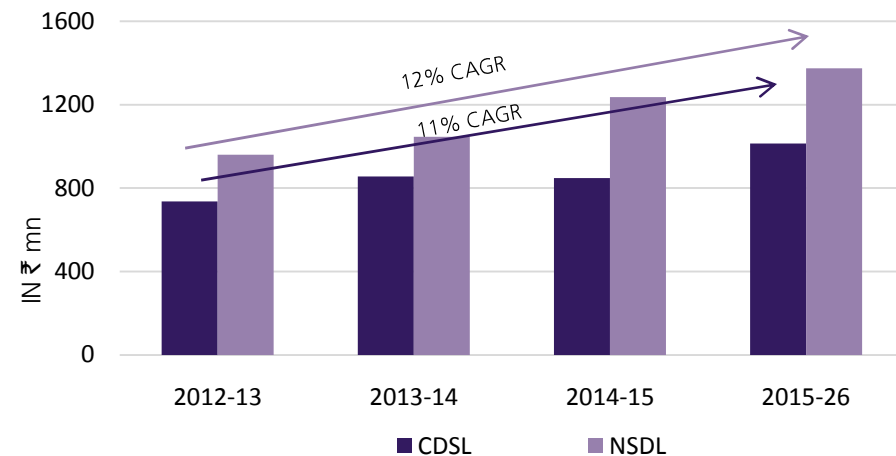
Source: Red Herring Prospectus, Destimoney Research

Industry Analysis: comparison between CDSL and NSDL

FY16-17 Market Share



Revenue Growth

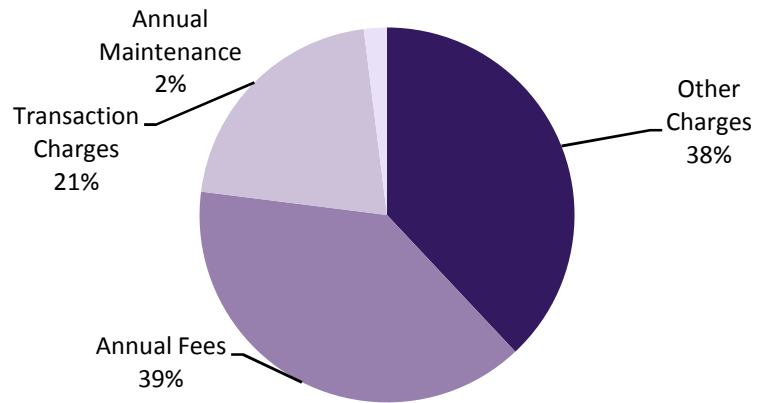


- ❑ The depository industry is a Rs 2.4Bn industry as of fiscal 2016 which has grown at a CAGR of ~12% over the last three fiscals. The industry comprises two 2 depositories , CDSL and NSDL. The industry has a strong entry barrier. This is due to the strong parental lineage enjoyed by the two depositories , CDSL being promoted by BSE and NSDL is being promoted by NSE and any new entrant will face stiff competition and will struggle to gain market share.
- ❑ CDSL has a 43% market share as per revenue and number of BO accounts as against NSDL’s 57%. It’s total revenue has been growing at CAGR ~11% over FY12-13 to FY15-17 as against ~12% of that of NSDL.
- ❑ The total number of accounts have been growing at CAGR 9% for CDSL and 5% for NSDL over the same period, standing at 14.57Mn
- ❑ accounts at NSDL and 10.79Mn accounts at CDSL.
- ❑ The charges structure for both depositories are vastly identical.
- ❑ The equity cash turnover on BSE and NSE rose from 323.5Mn to 407.5Mn trades and 1437.7 Mn to 1851 Mn trades respectively. Such increase in equity cash turnover is beneficial for the company as more shares change hands which is the responsibility of the company to handle as a depository.

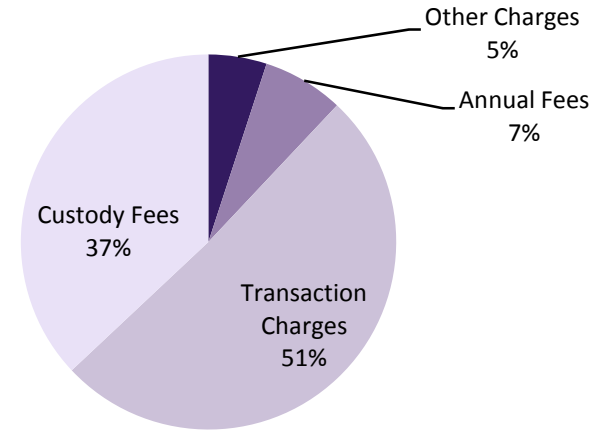
Source: Red Herring Prospectus

Industry Analysis: comparison between CDSL and NSDL

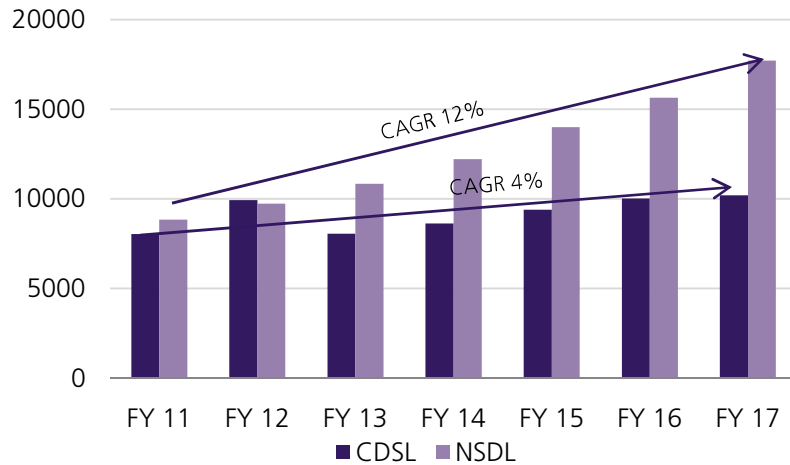
CDSL Revenue from operations for FY16



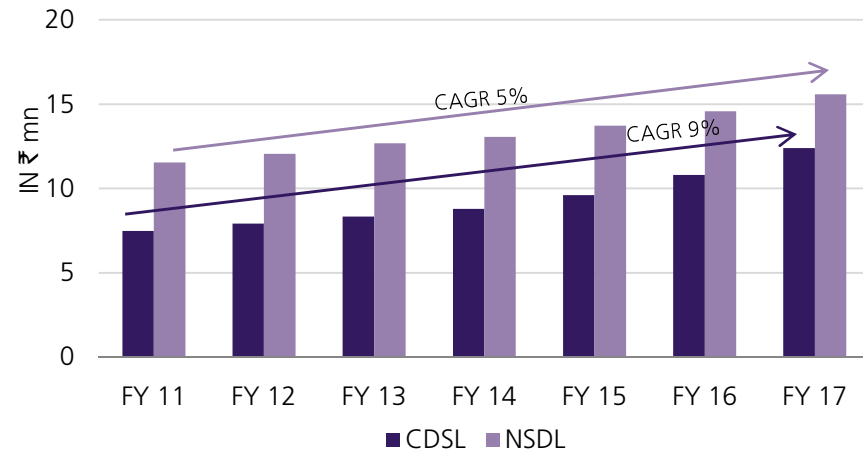
NSDL Revenue from operations for FY16



No of companies available in demat



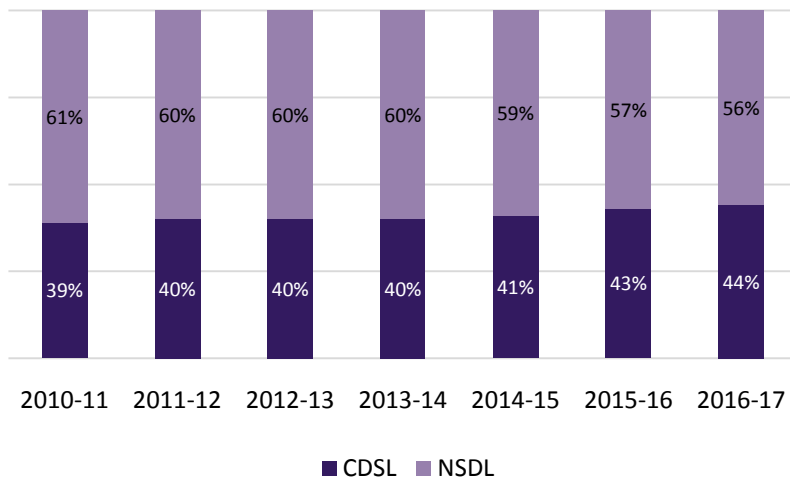
NO. of BO accounts in India



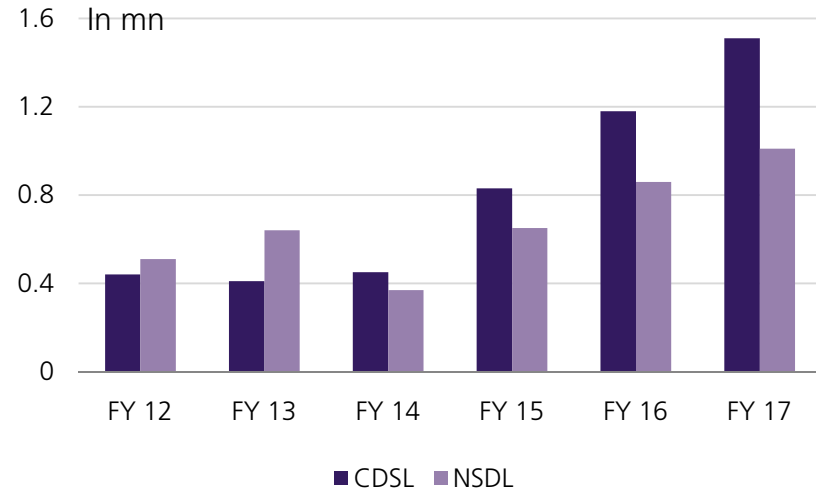
Source: Red Herring Prospectus, Destimoney Research

Industry Analysis: comparison between CDSL and NSDL

Market share of Demat accounts of CDSL and NSDL



Number of incremental demat accounts



- In terms of market share of demat accounts, CDSL has been growing at a higher rate with a CAGR of 9%, compared with 5% for NSDL. CDSL has experienced a growth in market share from 39% in Fiscal 2011 to 44% in Fiscal 2017.
- Consequently, CDSL has gained in market share with respect to incremental demat accounts from 46% in Fiscal 2012 to 60% in Fiscal 2017.

Source: Red Herring Prospectus, Destimoney Research

Major Shareholders of CDSL

| Name of the Shareholder | No. of Equity Shares | Percentage(%) |
|-------------------------------------|----------------------|---------------|
| BSE Limited | 5,22,97,850 | 50.05% |
| State Bank Of India | 1,00,00,000 | 9.57% |
| HDFC Bank Limited | 75,00,000 | 7.18% |
| Standard Chartered | 75,00,000 | 7.18% |
| Canara Bank | 67,44,600 | 6.45% |
| Bank Of India | 58,20,000 | 5.57% |
| Bank Of Baroda | 53,00,000 | 5.07% |
| Life Insurance Corporation of india | 43,36,750 | 4.15% |
| Union Bank Of India | 20,00,000 | 1.91% |
| Bank Of Maharashtra | 20,00,000 | 1.91% |
| | 10,34,99,200 | 99.04% |

Source: Red Herring Prospectus, Destimoney Research

Consolidated Summary Financials

Income Statement

| ₹ mn | FY17 | FY16 | FY15 | FY14 | FY13 |
|---------------------------------|--------------|--------------|------------|------------|------------|
| Total Income | 1,460 | 1,229 | 1,053 | 889 | 908 |
| Operating Expense | 664 | 578 | 590 | 562 | 550 |
| EBIDTA | 796 | 650 | 463 | 327 | 357 |
| Depreciation | 39 | 53 | 74 | 50 | 26 |
| Other Income | 409 | 385 | 402 | 339 | 333 |
| Exceptional items (Net) | - | 331 | 17 | - | - |
| PBT | 1,166 | 1,313 | 808 | 616 | 664 |
| Tax | 300 | 402 | 233 | 127 | 154 |
| PAT(Before extraordinary items) | 866 | 911 | 575 | 490 | 510 |
| Extraordinary Items net of tax | - | - | - | - | - |
| Net Profit | 866 | 911 | 575 | 490 | 510 |

| ₹ mn | FY17 | FY16 | FY15 | FY14 | FY13 |
|---------------|-------|-------|-------|-------|-------|
| EBIDTA Margin | 54.5% | 52.9% | 44.0% | 36.8% | 39.4% |
| Net Margin | 59.3% | 74.2% | 54.6% | 55.1% | 56.2% |
| ROE | 16.2% | 19.0% | 13.8% | 13.9% | 15.5% |
| ROCE | 21.2% | 19.7% | 18.3% | 15.9% | 18.3% |

Balance Sheet

| ₹ mn | FY17 | FY16 | FY15 | FY14 | FY13 |
|-------------------------------------|--------------|--------------|--------------|--------------|--------------|
| Liabilities | | | | | |
| Share capital | 1,045 | 1,045 | 1,045 | 1,045 | 1,045 |
| Reserves and surplus | 4,288 | 3,748 | 3,115 | 2,489 | 2,240 |
| Minority Interest | 155 | 147 | 146 | 136 | 124 |
| Other long term liabilities | 6 | 5 | 3 | 218 | 216 |
| Deferred Tax Liabilities | 7 | 29 | 10 | 0 | 0 |
| Secured Loans | 0 | 0 | 0 | 0 | 0 |
| Trade payables | 90 | 73 | 71 | 55 | 52 |
| Other current liabilities | 405 | 432 | 706 | 339 | 215 |
| Short-term provisions | 76 | 50 | 18 | 276 | 275 |
| Total Liabilities | 6,073 | 5,530 | 5,115 | 4,558 | 4,166 |
| Assets | | | | | |
| Net Block | 52 | 37 | 67 | 96 | 85 |
| CWIP | 0 | 0 | 0 | 2 | 9 |
| Intangible Assets Under Development | 3 | 0 | 0 | 0 | 4 |
| Long term loans and advances | 1 | 0 | 1 | 137 | 115 |
| Non- Current Investment | 2,729 | 2,105 | 2,232 | 447 | 258 |
| Other Non- Current Investment | 227 | 297 | 345 | 0 | 0 |
| Deferred Tax Asset | 23 | 0 | 8 | 39 | 46 |
| Current Investments | 2,300 | 2,470 | 1,909 | 3,307 | 3,162 |
| Trade receivables | 133 | 130 | 69 | 62 | 85 |
| Cash & bank balances | 483 | 404 | 431 | 410 | 353 |
| Short-term loans and advances | 1 | 1 | 1 | 22 | 24 |
| Other Current Assets | 121 | 87 | 51 | 35 | 25 |
| Total Assets | 6,073 | 5,530 | 5,115 | 4,558 | 4,166 |

Source: Red Herring Prospectus

Key Risks

- ❑ Heavily IT dependant. The business of the company is heavily IT dependant and any malfunction or hitches in the IT infrastructure may have a considerable impact in the workings of the business. Due to the nature of the highly customized nature of the company's equipment and systems, the revival of the system after a malfunction may be difficult. Any malfunction may cause material losses to the clients thereby making the company susceptible to litigation.
- ❑ Shift in preference from investing and trading activities to alternate securities. If there is a shift from delivery based trading to other securities which may not require the services of the depository, it may lead to a substantial decline in revenue for the depository. The company's revenue may also be effected by a change in investor confidence in the markets because a decline in volumes will have an adverse impact on the company's revenue. Because the source of revenue of the company is directly linked to the markets, its delivery based revenues will face high uncertainty.
- ❑ Rapid Changes in the IT environment.
- ❑ A failure to react to changes in the IT environment before its competitor may result in a decrease in market share of the company. This also applies to failing to upgrade systems to match customer requirements and satisfaction.
- ❑ The industry faces vast regulatory oversight. The industry in which the company operates faces high regulatory oversight and such excessive regulation may prove to be adverse for the company if such regulations are tightened further. The company also requires an array of permissions and approvals in the normal course of its business and the inability to obtain the same may have an adverse impact on the business.

Source: Red Herring Prospectus, Destimoney Research

Destimoney Securities Private Limited

6th Floor, " A " Wing , Tech-Web Centre, New Link Road, Oshiwara , Near Behram Baug, Jogeshwari (West), Mumbai - 400102

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