

GEOJIT FINANCIAL SERVICES

INR 105



Partnering growth

NOT RATED

Geojit Financial Services (Geojit) reported strong set of numbers in Q3FY08, buoyed by: (1) industry-wide surge in equity trading volumes; (2) increased traction in its distribution business; and (3) significant scale up in its Gulf JV (Barjeel Geojit).

Consolidated revenues recorded 59% growth Q-o-Q to INR 809 mn (more than double Y-o-Y), primarily driven by 73% Q-o-Q growth in equity broking revenues, 77% rise in revenues from Barjeel Geojit, and 33% growth in financial products distribution.

Geojit's operating margin improved 280bps sequentially to 43.2% in Q3FY08 due to better operating leverage. Consequently, net profit jumped 78% Q-o-Q to INR 222 mn.

* **Equity broking business: Revenues supported by surging volumes and better yields**

The company's equity broking revenues surged 73% Q-o-Q to INR 603 mn, as average daily trading volumes in Q3FY08 almost doubled to INR 10.5 bn (from INR 5.6 bn for H1FY08). Even blended commission yields improved to 9.1bps in Q3FY08 from 8.35 in H1FY08 as the proportion of cash delivery transactions in total volumes rose from 11% to 14%; the proportion of cash and derivatives segment remained almost steady at 43:57. In 9MFY08, broking revenues grew by 83% Y-o-Y to INR 1.2 bn, constituting 70% of revenues. We expect volumes to further gain traction with expanded presence in North and West India and entry in to institutional broking and margin funding.

* **Commodity broking: Volumes adversely affected by regulatory changes**

Geojit's commodity broking revenue registered a decline of 35% Y-o-Y in Q3FY08 to INR 28 mn on account of regulatory changes related to quantitative restrictions on broker-wise and customer-wise agri commodities exposure. We have assumed 35% decline in commodity revenues for FY08. The company expects these quantitative restrictions in select commodities to be lifted by the regulator in February and post this development, its commodities broking business is likely to gain traction.

* **Distribution business: Gaining traction**

Geojit is significantly scaling up its distribution business and the number of employees involved in sales/distribution has gone up from 184 in FY06 to 453 in H1FY08. It plans to add ~400 people every year in this business. It has generated distribution income of INR 49 mn in Q3FY08 (33% growth Q-o-Q) and of INR 114 mn in 9MFY08 (85% growth Y-o-Y). Mutual fund distribution dominates the pie, constituting more than 90% of distribution revenues. The company expects to end this fiscal with INR 200 mn of distribution income. Going forward, the company intends to grow this fee-based stream aggressively to ~18-20% of revenues.

Financials

Year to March	Q3FY08	Q3FY07	Growth (%)	Q2FY08	Growth (%)	FY07	FY08E
EBTIDA (INR mn)	350	109	222.1	206	69.8	432	1,070
Net profit (INR mn)	222	67	233.0	125	77.8	252	685
BV per share (INR)						10.1	12.0
EPS (INR)	1.0	0.4	136.4		NA	1.6	2.8
Price/ Book (x)						10.3	8.7
Price/ Earnings (x)						65.4	37.7

January 11, 2008

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Market Data

52-week range (INR) : 118 / 30
Share in issue (mn) : 209.0
M cap (INR bn/USD mn) : 21.9 / 557.7
Avg. Daily Vol. BSE ('000) : 700.3

Share Holding Pattern (%)

Promoters : 58.6
MFs, Fls & Banks : 4.3
Fls : 2.2
Others : 34.9

* **Rapid scale up in Middle East**

The company is also seriously looking at opportunities in the Middle East, where there is abundant investible surplus and liquidity of funds (petro dollars). Its JV with the Al-Saud Group in the UAE is rapidly scaling up and now serves 35,000 clients through five branches and 80 employees. Geojit's 30% share in the JV's income and profit in Q3FY08 was equivalent to INR 26 mn and INR 14 mn, respectively. The company plans to add 30-40 employees and two branches in the near term and we expect significant profitability from this JV going forward.

In addition, the company is exploiting opportunities in the Gulf by expanding its presence through three more joint ventures:

- ◆ **Aloula Geojit:** First Indian broking firm to offer broking services in local markets of Saudi Arabia.
- ◆ 49:51 JV in Dubai to deal in UAE-listed shares in the Dubai financial market, IPOs, and third party distribution of UAE funds, with an initial investment of ~INR 161 mn.
- ◆ Tie up with the Bank of Bahrain and Kuwait, the largest retail bank in Bahrain, for providing investment services to NRIs.

* **Other highlights**

- ◆ Operating expenses have increased by 64% Q-o-Q to INR 207 mn on account of higher business associate's commission of INR 119 mn paid during the quarter (against INR 65 mn in Q2FY08).
- ◆ It currently manages PMS portfolio worth ~INR 850 mn and has booked fees of INR 23 mn in 9MFY08. It is expected to leverage the fund management expertise of BNP Paribas and its relationship with NRIs to scale up this business phenomenally, going forward.
- ◆ It has received a software consultancy contract from BNP Paribas for setting up the JV's back office and front office operations and in this regard, has received part payment of consultancy fees of INR 10 mn during the quarter.

* **Outlook and valuation: Positive; new partnerships to add value**

We believe Geojit is transforming itself from being a plain vanilla regional retail broking firm to a full service pan-India brokerage house. We expect its revenues to grow by 72% CAGR over FY07-09E and it is likely to report EPS of INR 2.8 in FY08E and INR 4.5 in FY09E. Its revenue growth will be led by industry-wide growth in trading volumes, entry into institutional broking, successful roll out of operations in Saudi Arabia and UAE, and aggressive scale up of distribution and PMS services. The stock is currently trading at 23x FY09E earnings, which is at a discount to its peers. We have a positive view on the stock. The stock is currently not under our coverage.

(INR mn)

Financial snapshot								
Year to March	Q3FY08	Q3FY07	Growth (%)	Q2FY08	Growth (%)	FY07	FY08E	FY09E
Operating income								
- Brokerage related income	656	302	117.4	396	65.6	1,111	2,035	2,733
Equity brokerage	603	242	148.9	349	73.0	878	1,845	2,496
Commodity brokerage	28	43	(35.1)	28	(1.4)	175	114	142
Depository services	25	17	51.0	19	30.3	58	76	95
- Financial product distribution	49	20	151.8	37	33.3	96	191	344
- Portfolio management services	9	5	81.0	8	13.8	21	36	62
- Interest income from credit	7	0	NA	8	(6.8)	0	40	61
- Share of JVs*	26	12	122.0	15	77.2	37	84	553
- Interest from margin funding	5	2	146.5	3	62.9	7	19	161
- Others	33	8	305.2	14	141.8	40	52	104
Total operating income	787	349	125.6	481	63.6	1,312	2,457	4,018
Other income	22	6	304.7	29	(24.1)	49	75	23
Total revenues	809	354	128.4	510	58.5	1,361	2,532	4,041
Expenses								
- Operating expenses	207	113	84.0	127	63.6	392	634	860
- Employee cost	158	78	102.5	113	40.3	267	480	763
- Share of JVs*	13	1		2	676.3	20	54	376
- Administrative and other expenses	81	54	50.5	63	28.0	249	294	368
Total expenses	459	245	87.0	304	50.9	929	1,461	2,366
EBITDA	350	109	222.1	206	69.8	432	1,070	1,675
Interest and other financing charges	1	0	NA	0	710.7	2	12	30
Depreciation	22	13	76.1	22	(0.6)	52	91	100
PBT	327	96	240.4	184	78.0	378	967	1,545
Taxes	102	31	228.1	58	76.3	134	323	510
PAT	225	65	246.3	126	78.8	244	644	1,035
Add : Share of profit from associates	0	2	(100.0)	0	NA	8	0	0
Less: Minority interest in the shareholding	3	0	NA	4	(29.4)	0	0	0
Dividend on pref. share capital (net of tax)			NA		NA	0	0	0
Exceptional items (net of tax)	0	0	NA	3	(100.0)	0	40	0
Adjusted PAT	222	67	233.0	125	77.8	252	685	1,035
Diluted EPS (INR)	1.0	0.4	136.4	0.6	77.8	1.6	2.8	4.5
Ratios (%)								
EBITDA margin	43.2	30.7		40.4		31.7	42.3	41.4
PBT margin	40.4	27.1		36.0		27.8	38.2	38.2
PAT margin	27.5	18.9		24.5		18.5	27.0	25.6
Tax rate	31.2	32.3		31.5		35.4	33.4	33.0

Company Description

Geojit, incorporated in 1987, offers a bouquet of financial products and services to retail investors—equity and commodity broking, portfolio management services, and third party distribution of mutual funds and insurance. The company has established a strong network in South India and is planning to increase its presence in West and North India. It caters to 0.4 mn customers through its network of 415 offices.

While brokerage income remains a major contributor to revenue and profitability, income from commodity and distribution business is gaining traction. The company also provides portfolio management services and manages a corpus of more than INR 850 mn. It offers commodity broking through its subsidiary Geojit Commodities. Value-added services like customized finance and structured credit facilities in association with Geojit Credits Private had its impact in the volume building exercise.

Promoters hold 58% (including C J George and Shiny George at 22%, KSIDC 9%, and BNP Paribas 27%), while FIIs have 2.2% stake in the company.

Investment Theme

We believe Geojit is transforming itself from being a plain vanilla regional retail broking firm to a full service pan-India brokerage house. It has taken several initiatives in this direction:

- Expanding its presence in North and West India; targets 85 and 100 new branches (owned) in CY08 and CY09, respectively.
- Formed 50:50 JV with BNP Paribas Securities Asia for an institutional broking business.
- Will actively focus on margin funding activities from Q4FY08 through a separate NBFC.
- Leverage its network and NRI client base for third party distribution.
- Leverage on fund management expertise of BNP Paribas and its relationship with NRIs to significantly scale up its PMS services.

Besides India, Geojit is also seriously looking at opportunities in the Middle East, where there is abundant investible surplus and liquidity of funds (petro dollars). It already has leadership position in the UAE, among NRIs interested in investing in the Indian market through Barjeel Geojit Securities, and is now expanding its presence in the Gulf through three joint ventures.

Key Risks

* Highly leveraged to capital market

The company's businesses are dependent on the conditions of the capital market and any unfavourable developments in the market, affecting investor sentiments can significantly hamper revenue growth.

* Highly competitive nature of industry

The brokerage industry is highly competitive and can affect Geojit's plans of pan-India presence. Dip in market share and margin due to competition can affect the company's profitability.

* Execution risk in newly launched business

Its institutional broking and gulf businesses are expected to be launched and scaled up in the next few quarters and execution risk exist in these ventures, which can adversely affect profitability.

Financial Statements

Income statement					(INR mn)
Year to March	FY05	FY06	FY07	FY08E	FY09E
Operating income					
- Brokerage related income	495	876	1,111	2,035	2,733
Equity brokerage	430	733	878	1,845	2,496
Commodity brokerage	55	82	175	114	142
Depository services	11	61	58	76	95
- Financial product distribution	13	65	96	191	344
- Portfolio management services	4	16	21	36	62
- Interest income from credit				40	61
- Share of JVs*	13	36	37	84	553
- Interest from margin funding	-	0	7	19	161
- Others	2	17	40	52	104
Total operating income	528	1,010	1,312	2,457	4,018
Other income	11	9	49	75	23
Total revenues	538	1,020	1,361	2,532	4,041
Expenses					
- Operating expenses	151	281	392	634	860
- Employee cost	92	178	267	480	763
- Share of JVs*	6	16	20	54	376
- Administrative and other expenses	111	174	249	294	368
Total expenses	361	649	929	1,461	2,366
EBITDA	177	370	432	1,070	1,675
Interest and other financing charges	0	0	2	12	30
Depreciation	25	39	52	91	100
PBT	152	331	378	967	1,545
Taxes	54	107	134	323	510
PAT	98	224	244	644	1,035
Add : Share of profit from associates	-	3	8	-	-
Div. on pref. share capital (net of tax)	3	-	-	-	-
Exceptional items (net of tax)				40	
Adjusted PAT	95	227	252	685	1,035
Diluted EPS (INR)	0.7	1.5	1.6	2.8	4.5
DPS (INR)	0.2	0.4	0.4	1.0	1.3

* JVs include institutional broking business; Barjeel Geojit and Aloula Geojit

Growth ratios (%)

Year to March	FY05	FY06	FY07	FY08E	FY09E
Revenue growth	32.0	89.5	33.5	86.0	59.6
Expenses growth	52.7	80.0	43.1	57.3	61.9
EBITDA growth	3.6	108.8	16.7	147.7	56.5
PBT growth	0.0	117.8	14.1	155.9	59.8
PAT growth	(0.4)	139.5	11.0	171.5	51.2

Operating ratios (%)

Year to March	FY05	FY06	FY07	FY08E	FY09E
Broking income / Total income	92.0	85.9	81.7	80.4	67.6
Operating expenses/ Total income	28.1	27.6	28.8	25.0	21.3
Employee cost / Total income	17.1	17.5	19.6	18.9	18.9
Other expenses / Total income	21.7	18.6	19.8	13.8	18.4
EBITDA margin	33.0	36.3	31.7	42.3	41.4
PBT margin	28.3	32.5	27.8	38.2	38.2
PAT margin	18.2	22.0	17.9	25.4	25.6

Balance sheet					(INR mn)
Year to March	FY05	FY06	FY07	FY08E	FY09E
Liabilities					
Equity capital	152	152	209	209	232
Reserves	176	333	1,908	2,295	3,538
Networth	328	485	2,117	2,504	3,770
Monies pending allotment	-	-	85	85	-
Employee stock options outstanding	-	0	4	4	4
Secured loans	-	-	-	-	1,680
Deferred tax liability	13	19	24	37	58
Total	341	504	2,231	2,631	5,512
Assets					
Fixed assets	134	220	253	283	289
Investments	121	118	413	1,048	1,200
Current Assets					
- <i>Sundry debtors</i>	164	352	409	760	1,023
- <i>Cash and bank balances</i>	285	487	1,826	2,607	4,319
- <i>Loans and advances</i>	418	960	1,139	1,656	4,298
- <i>Others</i>	3	2	18	27	39
Current liabilities					
- <i>Current liabilities</i>	697	1,448	1,561	2,903	3,910
- <i>Provisions</i>	90	192	271	851	1,751
Net current assets	82	162	1,559	1,295	4,018
Goodwill	4.1	3.8	4.8	4.8	4.8
Miscellaneous expenses not written off	0	-	-	-	-
Total	341	504	2,231	2,631	5,512

Valuation metrics (%)

Year to March	FY05	FY06	FY07	FY08E	FY09E
EPS (INR)	0.7	1.5	1.6	2.8	4.5
<i>EPS growth (%)</i>	10.1	107.6	7.5	73.3	60.6
Book value per share (INR)	2.2	3.2	10.1	12.0	16.3
RoE (%)	37.0	55.9	19.4	29.6	33.0
Price/Earnings (x)	145.8	70.2	65.4	37.7	23.5
Price/ BV (x)	48.7	32.9	10.3	8.7	6.4
Dividend yield (%)	0.2	0.4	0.4	0.9	1.3

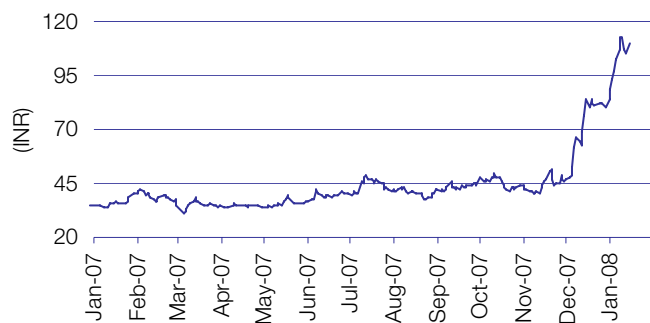
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Geojit Financial Services



Recent Research

Date	Company	Title	Price (INR)	Recos
10-Jan-08	Future Capital	Future lies in execution; IPO Note	700-765	Subscribe
9-Jan-08	Axis Bank	Fast and the furious, discovering value Visit Note	1,096	Buy
09-Jan-08	ICICI Bank	Bank on non-banking; Visit Note	1,310	Buy
09-Jan-08	Banking	Improving margins; ride The equity wave; Sector Update		

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Accumulate	Reduce	Sell	Total
Rating Distribution*	107	45	18	3	193

* 13 stocks under review /3 rating withheld

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	104	69	20

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 20% over a 12-month period
Accumulate	appreciate up to 20% over a 12-month period
Reduce	depreciate up to 10% over a 12-month period
Sell	depreciate more than 10% over a 12-month period

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