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# CHALLENGES OF MID-LEVEL FINANCIAL HOUSES

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# Agenda

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- ❑ What is a financial house?
  - ❑ What is a mid-level financial house?
  - ❑ Business distribution in the market
  - ❑ Challenges faced
  - ❑ Way Ahead
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What is a financial house?

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# What is a financial house?

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- Merchant banker and/or an investment banker
  - Stock broker
  - Depository Participant
  - Portfolio Manager
  - Custodians
  - Registrars and transfer agents.
  - AMC/Mutual funds
  
  - Exceptions
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What is a mid-level financial house?

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# What is a mid-level financial house?

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A mid size financial house is the one which :

- Offers all or most of the services mentioned above in its company or as a group
  - Is not part of a large Corporate house, Bank or Insurance company or FII
  - Is not a market leader in any of the services mentioned above
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# Business distribution in the markets



# Business distribution in the market

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## □ Unevenly distributed

- The business is very unevenly distributed between the large, mid sized and small intermediaries

## □ Some Interesting Facts:

- 22.5% of the total turnover is accounted for by the Top ten brokers of NSE from among the 1200 SEBI registered brokers of the Exchange across segments
  - 23.5 % of the total turnover for the exchange is accounted for by the Top ten brokers out of the total 450 SEBI registered brokers of BSE
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# Profitability analysis-stock broking

- ❑ During FY 10, a majority of broking houses had a significant improvement in operating profit margin (OPM)
- ❑ Overall OPM of the broking sample companies expanded 1468 bps y-o-y to 33.76%. OPM of large companies, which was the highest among the sample, expanded 1183 bps to 37.49%.
- ❑ Mid-size companies saw the highest improvement of 2247 bps to 30.52%. Small companies had the least OPM of 15.38% among the sample companies

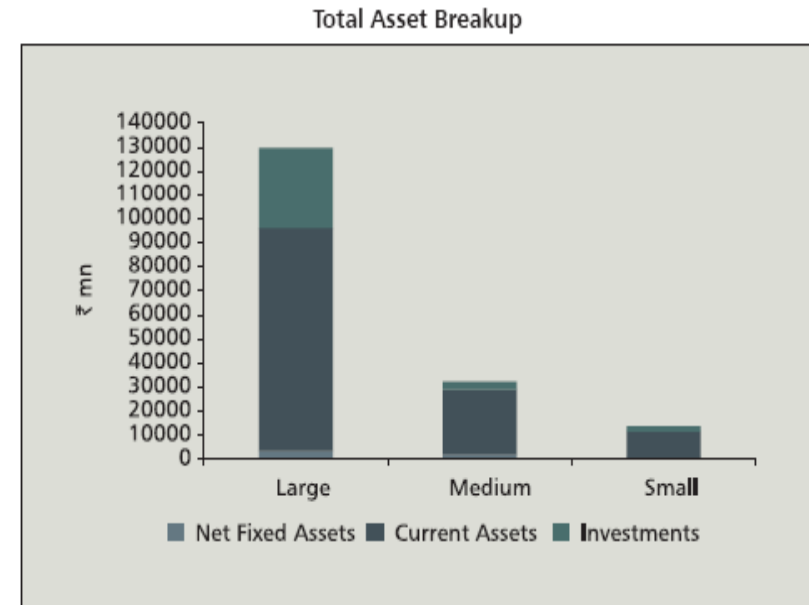
|        | FY08  |      | FY09  |      | FY10  |      |
|--------|-------|------|-------|------|-------|------|
| (%)    | OPM   | NPM  | OPM   | NPM  | OPM   | NPM  |
| Large  | 44.12 | 27.9 | 25.66 | 13.7 | 37.49 | 22.9 |
| Medium | 41.34 | 25.5 | 8.05  | 1    | 30.52 | 17   |
| Small  | 23.28 | 15.5 | -3.81 | -9.6 | 15.38 | 7.4  |

Source: Prowess, CMIE

# Assets break-up

Current assets and investments which are major assets of the broking companies had a total break up of 73% and 21.8% respectively in FY10

| Growth in Assets |            |                |            |
|------------------|------------|----------------|------------|
|                  | Large Co's | Mid-sized Co's | Small Co's |
| Total assets     | 19.1%      | 29.6%          | 36.4%      |
| Current assets   | 29.7%      | 37.5%          | 41.7%      |



Source: Prowess, CMIE

# Cost analysis-employee cost

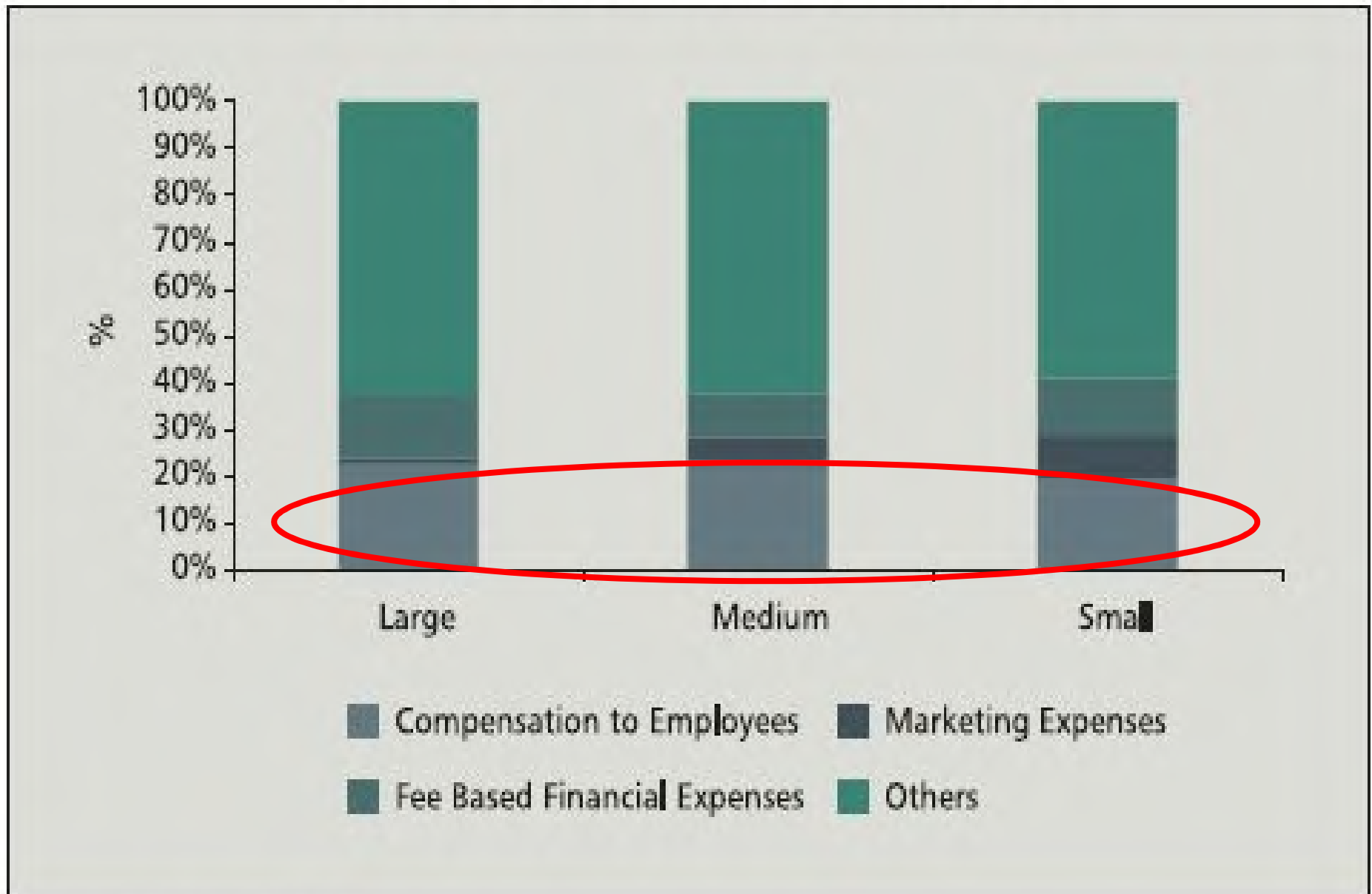
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- ❑ Major cost overheads of broking companies remained the same across all three categories during FY10.
- ❑ Employee compensation was the major cost, with aggregate share of 34.2% in overall expenses in FY10.
- ❑ Breakup of Employee Compensation category wise:

| S.No. | Category                  | Share of Employee Cost to Total Cost |
|-------|---------------------------|--------------------------------------|
| 1     | Large Broking Houses      | 34.1 %                               |
| 2     | Mid- Sized Broking Houses | 35.6 %                               |
| 3     | Small Broking Houses      | 30.4 %                               |

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## Cost Composition of Broking Companies



Source: Prowess, CMIE

# Mid-level financial houses

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- ❑ Covering 0.1 to 0.5% of the market share
  - ❑ Having a full fledged infra-structure
  - ❑ No mercy by the regulators
  - ❑ Trying for the best professionals
  - ❑ Squeezed by the client
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# Challenges faced by Mid-sized companies

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# Challenges faced by Mid-sized companies in the sector

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- Economy specific
  - Industry specific
  - Size specific
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# Economy specific

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- Over all bad market conditions
  - Effect of World economies
  - Inflation
  - War, national calamity or any other similar situation
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# Industry specific

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- ❑ Markets are very sentimental; react much faster than the economy in general
  - ❑ The volatile market conditions have a direct effect on the turnover
  - ❑ This directly affects not only the top lines of the financial houses but also their bottom lines.
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# Size specific-mid sized

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Costs :

- Infra structural cost
- Compliance cost
- Employee cost

Others:

- Competition from established Brands
  - Reputation
  - Sources of Finance - equity or debt route
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# What are the repercussions ?

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- ❑ Stunted Growth/ expansion
  - ❑ Inability to attract quality manpower
  - ❑ Costlier avenues of finance
  - ❑ Selling/Marketing challenges
    - Price war leading to shrinkage in brokerage rates
  - ❑ Regulator's perception
  - ❑ Escalating advertisement costs
  - ❑ Unequal economies of scale.
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# Exceptions-Inherent Advantages

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- ❑ Personal interest taken by the promoters
  - ❑ Higher Involvement-faster decision making
  - ❑ *The larger they are – the heavier they fall!*
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Way Ahead



# Way ahead

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- Stake Dilution
  - Mergers between the mid-sized players
  - In-organic growth
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Thank You!

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