# Capital Market

## F&O regulations: The cat's out of the bag

### Final measures tad better than consultation paper

- **SEBI has finally announced regulations to curb F&O volumes and strengthen the framework. Most of the measures are similar to the ones announced in the consultation paper released on 30th July'24.**
- **However, one measure from the consultation paper did not find a mention in the final regulation (rationalization of tick size) and two measures came in a relatively better form: 1) Minimum contract size increased to at least INR1.5m vs. INR2-3m in two phases in the consultation paper and 2) increase in extreme loss margin only on the expiry day at 2% vs. the 8% cumulative increase on pre-expiry and expiry day in the consultation paper.**
- **The regulations will be partially implemented from Nov'24 and, resultantly, the impact on volumes will be visible from Dec'24.**
- **Our sensitivity analysis yields nil earnings impact for Angel One in FY26 if the order volumes are down 10% vs. our assumption of 16% growth and the company is able to increase its realization from INR19.7 to INR25. We maintain our BUY rating on ANGELONE.**
- **Similarly, for BSE earnings, the hit would be miniscule if the derivative volumes decline by 20% instead of a 22% increase built in our forecasts and the premium to notional turnover ratio increases from 0.072% to 0.09%. We maintain our Neutral rating on BSE.**

### Angel One: Levers will be used at appropriate time to offset the profitability hit

- If all the measures listed in the consultation paper are included in the final regulations, turnover volumes for ANGELONE are likely to be impacted. However, it is difficult to ascertain the absolute impact at the current juncture.
- Most importantly, changes in customer behavior are difficult to predict. In the past, the allocation of customers' money from their wallets to trading activities has not changed meaningfully even after regulatory changes.
- Which measure to implement and the quantum of charges will be decided as and when they regulations are implemented and some impact is visible. Actions by competitors will be tracked closely before executing any of these steps. The choice for ANGELONE and its peers will be between 1) taking a hit on margins, leading to a higher market share, and 2) raising the charges and risking losing some market share in the interim.
- Important criteria before deciding on final actions for ANGELONE would be the impact on LTV of the customer from these regulations. Ideally, since the measures are aimed at reducing customer losses (if implemented), the longevity of the customer in the system increases. Additional products will only add to the LTV in the longer term, thus giving the company the ability to spend on higher acquisitions.

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- In FY26, if the number of orders for Angel One falls by 10% instead of 16% growth factored in our estimates and the company does not take a price hike or prune its customer acquisition costs, earnings will be down 33% as compared to our current estimate.
- Against this, if the company increases its average gross broking realization from INR19.7 to INR25, the impact on earnings will be largely nullified.
- The company demonstrated its willingness to protect profitability through the pricing action announced today (cash delivery broking charge increased from nil to INR20/order or 0.1% per executed order).
- In the past, the company has used customer acquisition as a variable lever to offset the impact in terms of slowdown in volumes.
- ANGELONE could see transitionary hit to earnings as the regulations are implemented and the company gauges the impact before making corrective actions. However, we believe the company is in a transformational phase wherein share of financial products distribution (loans and fixed income), wealth management and AMC, will start contributing meaningfully over the next couple of years. We retain our BUY rating on the stock.

**BSE: Product innovation will be key to offset the impact**

- BSE has scaled up its derivatives market share to 27%/13.3% in terms of notional turnover/premium turnover in Sep'24. This has been on the back of product innovation wherein they launched the expiries on different days vs the existing products of NSE.
- Large market share for BSE arises out of Sensex rather than Bankex. With now only one benchmark index will be available for launch of weekly expiry, NSE/BSE will continue with Nifty/Sensex. Earlier since NSE had an expiry on all days except Friday, BSE found it difficult to scale up volumes. Nevertheless, BSE will now have three more days to compete against NSE.
- Product innovation could be an alternative wherein new contracts can be launched on new indices with monthly expiries in different weeks.
- For BSE, since large volumes were happening on expiry day, its premium to notional turnover ratio was at 0.07% vs 0.16% for NSE (Sep'24). With probability of volumes increasing on farther than expiry days, this ratio would increase for BSE. This will not only help in revenues but also in bringing down the clearing and settlement costs.
- For FY26, if we assume notional ADTO to decline by 20% instead of a 22% increase factored in our current estimates, all other factors being the same, the earnings hit will be 9% for BSE. In our current estimates, the share of derivatives in overall revenues is 45% for BSE in FY26.
- If the premium to notional turnover for the options segment increases from 0.072% assumed in our forecast to 0.09%, as the volumes will start increasing farther from expiry, the impact will be nullified for BSE.
- Additional upsides could come from 1) the volume shift to cash segment and 2) if the premium to notional turnover increases, the clearing and settlement costs could decline
- BSE should be relatively lesser impacted in the new regulatory environment vs NSE. Furthermore, the exchange has other revenue drivers such as colocation segment and new products (commodities and power). We currently have a Neutral rating on the stock.

**Exhibit 1: Final regulations vs. recommendations in the consultation paper**

| Measure | Consultation paper | Final regulation | Better/Same/Worse |
|---|---|---|---|
| Rationalization of strike price | ❖ Recommended to reduce strikes | ❖ No mention | Better |
| Upfront collection of options premium | ❖ Members to collect option premiums on an upfront basis from clients | ❖ Implementation from Feb'25 | Same |
| Intraday monitoring of position limits | ❖ The position limits for index derivative contracts shall also be monitored by the clearing corporations/stock exchanges on an intra-day basis | ❖ Implementation from Apr'25 | Same |
| Removal of calendar spread benefit on the expiry day | ❖ Removal of the benefit was recommended | ❖ Implementation from Feb'25 | Same |
| Minimum contract size | ❖ To be increased in two phases 1) INR1.5m to INR2m and 2) after 6 months to INR2m to INR3m | ❖ Increased to minimum INR1.5m | Better |
| Rationalization of weekly index products | ❖ Weekly options contracts are to be provided on a single benchmark index of an exchange | ❖ Implementation from Nov'24 | Same |
| Increase in margin near contract expiry | ❖ 1) At the start of the day before expiry, Extreme Loss Margin (ELM) to be increased by 3%<br>❖ 2) At the start of the expiry day, ELM to be further increased by 5% | ❖ An additional ELM of 2% for short options contracts, implementation from Nov'24 | Better |

Source: MOFSL

**Exhibit 2: Impact on brokers and exchanges because of implementation of the measures**

| Measures | Brokers | Exchanges |
|---|---|---|
| Upfront collection of options premium | ❖ Already doing it, so relatively lesser hit | ❖ Impact on volumes, if smaller brokers are not collecting the premium upfront |
| Intraday monitoring of position limits | ❖ Compliance costs to increase a bit | ❖ Compliance costs to increase a bit |
| Removal of calendar spread benefit on the expiry day | ❖ Retail customers may not be using it materially and hence limited impact | ❖ HNIs and institutions will have to bring more margins and hence some volume hit can be envisaged, we expect more hit for NSE vs BSE |
| Minimum contract size | ❖ Largely retail base and hence impact in volumes can be material | ❖ Impact to the extent of retail volumes, HNI and institutional volumes should be relatively less impacted |
| Rationalization of weekly index products | ❖ Volumes could be hit as number of weekly expiries reduce, volumes could shift to other days or other segments (cash/commodities) | ❖ NSE has larger number of weekly expiries and hence a relatively larger hit, BSE could see lesser hit as volume hit of Bankex volumes can be offset by higher volumes on other days |
| Increase in margin near contract expiry | ❖ Largely retail base who are buyers of options and hence no material impact | ❖ HNIs and institutions will have to bring more margins and hence some volume hit can be envisaged |

Source: MOFSL

**Exhibit 3: Angel One FY26 PAT sensitivity to Revenue per order and change in number of orders**

| | | Revenue per order | | | | | | |
|---|---|---|---|---|---|---|---|---|
| No of orders | Change vs FY25 | 19.7 | 20.7 | 21.7 | 22.7 | 23.7 | 24.7 | 25.7 |
| 1,191 | -40% | 5,125 | 5,778 | 6,432 | 7,085 | 7,738 | 8,391 | 9,044 |
| 1,390 | -30% | 7,269 | 8,031 | 8,793 | 9,554 | 10,316 | 11,078 | 11,840 |
| 1,588 | -20% | 9,412 | 10,283 | 11,154 | 12,024 | 12,895 | 13,766 | 14,636 |
| 1,787 | -10% | 11,555 | 12,535 | 13,515 | 14,494 | 15,474 | 16,453 | 17,433 |
| 1,985 | 0% | 13,699 | 14,787 | 15,876 | 16,964 | 18,052 | 19,141 | 20,229 |
| 2,184 | 10% | 15,842 | 17,039 | 18,237 | 19,434 | 20,631 | 21,828 | 23,026 |
| 2,303 | 16% | 17,128 | 18,391 | 19,653 | 20,916 | 22,178 | 23,441 | 24,703 |
| 2,581 | 30% | 20,129 | 21,544 | 22,959 | 24,373 | 25,788 | 27,203 | 28,618 |
| 2,780 | 40% | 22,272 | 23,796 | 25,320 | 26,843 | 28,367 | 29,891 | 31,415 |

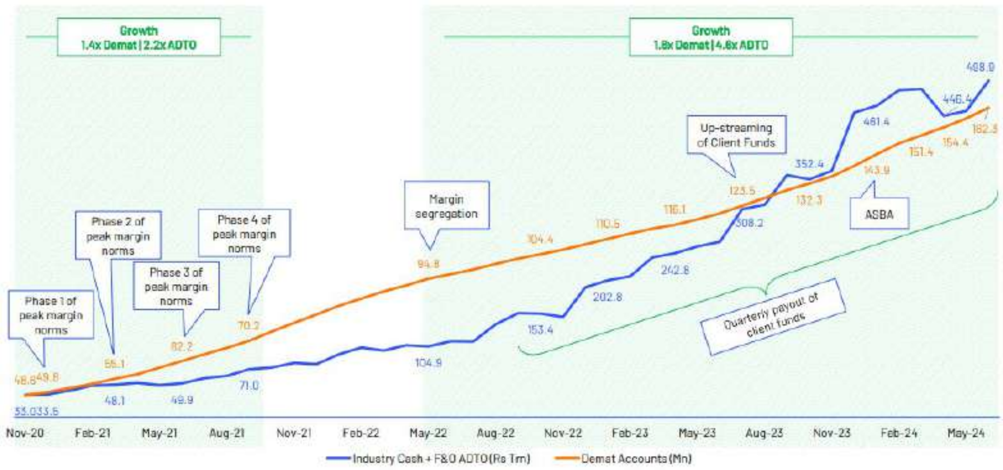
Source: Company, MOFSL

**Exhibit 4: BSE FY26 PAT sensitivity to change in derivatives segment ADTO and Premium/Notional Turnover ratio**

| | | Premium/Notional turnover ratio | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **13,449** | **0.06** | **0.07** | **0.08** | **0.09** | **0.1** | **0.11** | **0.12** |
| Change in notional turnover | -20 | 11,434 | 12,254 | 12,768 | 13,435 | 14,102 | 14,769 | 15,436 |
| | -10 | 11,615 | 12,538 | 13,116 | 13,866 | 14,616 | 15,367 | 16,117 |
| | - | 11,797 | 12,822 | 13,464 | 14,298 | 15,131 | 15,965 | 16,798 |
| | 10 | 11,978 | 13,105 | 13,812 | 14,729 | 15,646 | 16,563 | 17,480 |
| | 22.1 | 12,197 | 13,449 | 14,233 | 15,251 | 16,269 | 17,287 | 18,305 |
| | 30 | 12,340 | 13,673 | 14,508 | 15,592 | 16,675 | 17,759 | 18,843 |
| | 40 | 12,522 | 13,957 | 14,856 | 16,023 | 17,190 | 18,357 | 19,524 |

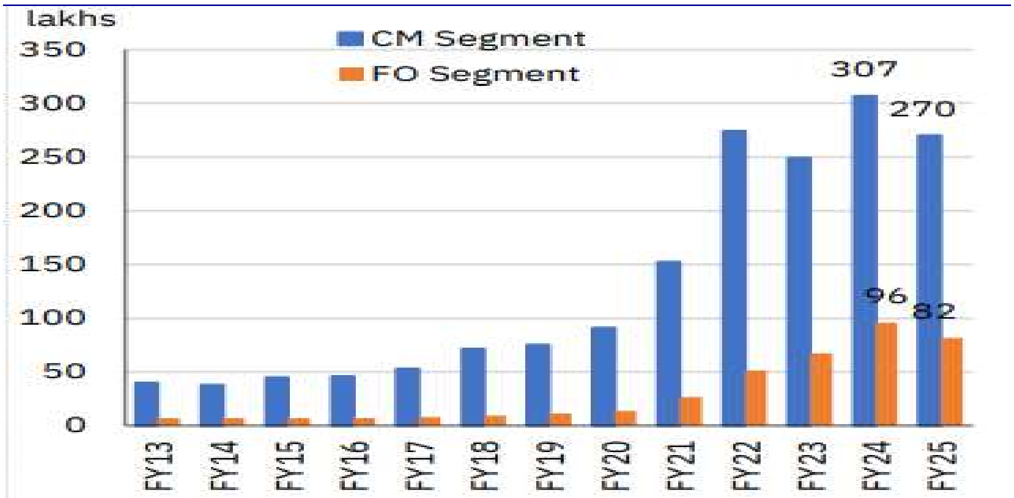
Source: Company, MOFSL

**Exhibit 5: Demat account addition and ADTO trends have sustainably remained strong in spite of several regulatory changes in the past few years**



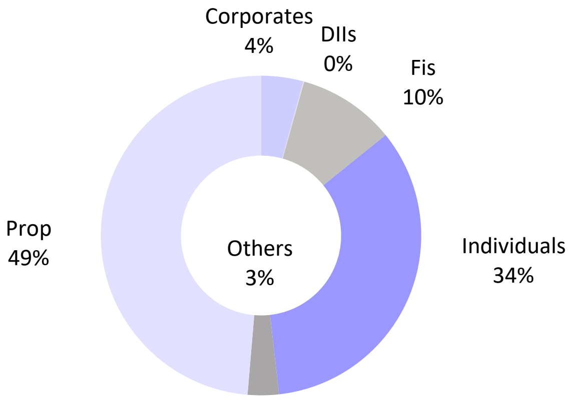

Source: Company, MOFSL

**Exhibit 6: Number of retail customers in cash segment and F&O segment**




Source: NSE, MOFSL

**Exhibit 7: Share of individuals is at 34% in premium turnover on YTD basis**



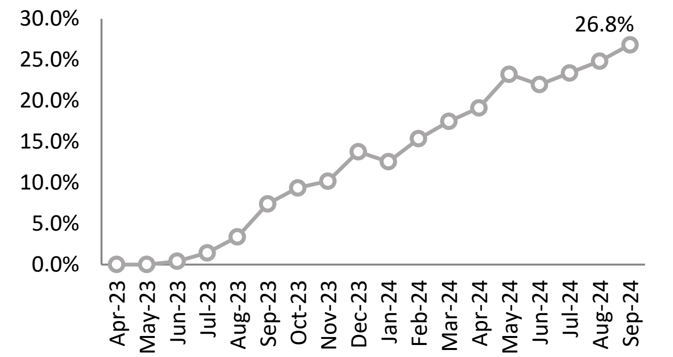

Source: NSE, MOFSL

**Exhibit 8: 46% of the customers trade in less than INR100k premium turnover during a month and their share in premium turnover is 0.3%**

| Premium turnover range INR | Turnover INR b | Share in Turnover % | Unique investors m | Share in investors m |
|---|---|---|---|---|
| <10k | 1 | 0 | 0.92 | 20.2 |
| 10k-100k | 25 | 0.2 | 1.18 | 25.9 |
| 100k-1m | 276 | 2 | 1.44 | 31.6 |
| 1m-10m | 1,322 | 9.6 | 0.83 | 18.2 |
| 10m-100m | 2,197 | 15.9 | 0.17 | 3.7 |
| >100m | 9,985 | 72.3 | 0.01 | 0.2 |
| **Total** | **13,807** | | **4.55** | |

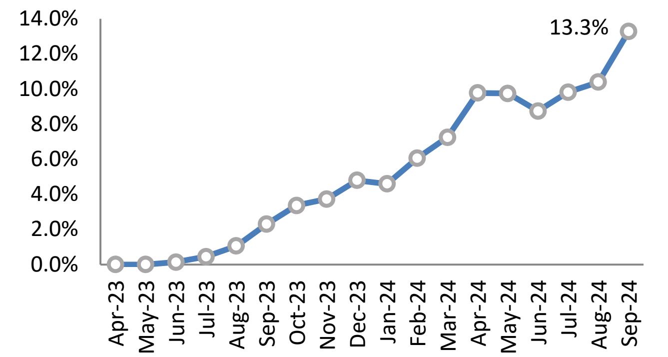
Source: NSE, MOFSL

**Exhibit 9: BSE's market share trend in notional turnover**



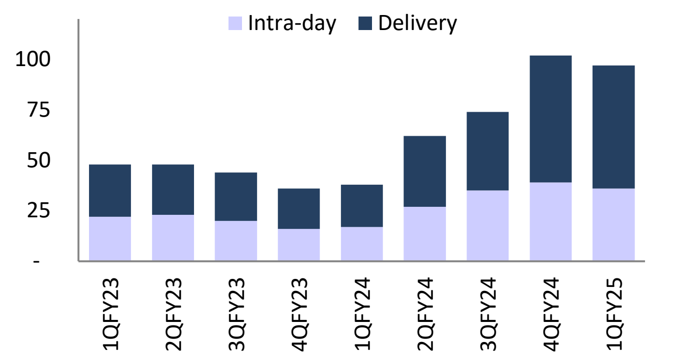

Source: Company, MOFSL

**Exhibit 10: BSE's market share trend in premium turnover**



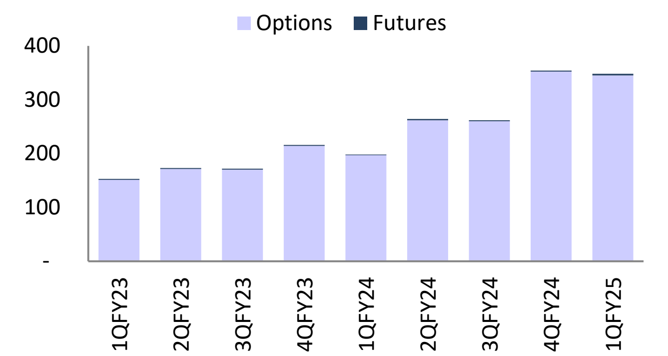

Source: Company, MOFSL

**Exhibit 11: Angel One order mix in cash segment**



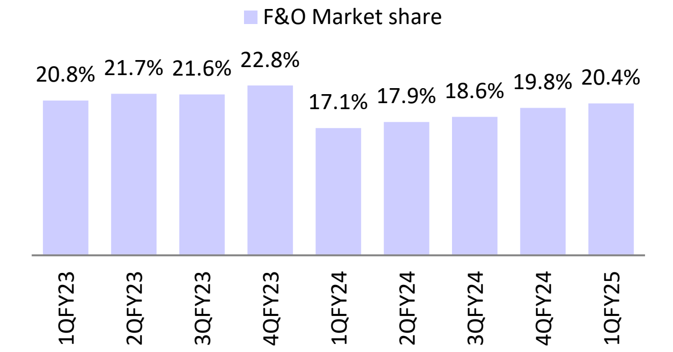

Source: Company, MOFSL

**Exhibit 12: Angel One order mix in F&O segment**



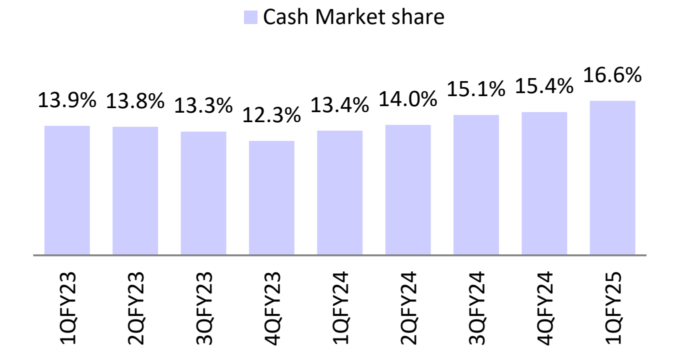

Source: Company, MOFSL

**Exhibit 13: Angel One F&O Market share**




Source: Company, MOFSL

**Exhibit 14: Angel One Cash segment market share**




Source: Company, MOFSL

Market share prior to 1QFY24 is based on notional turnover for options and post that it is based on premium turnover

| Explanation of Investment Rating | |
|---|---|
| **Investment Rating** | **Expected return (over 12-month)** |
| BUY | >=15% |
| SELL | < - 10% |
| NEUTRAL | < - 10 % to 15% |
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