Twitter Thread by Dinesh Sairam

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This thread is for investors or those who are interested in CDSL as an investment. Often the central reason quoted for an investment here is the gush of FCF the business produces and some float money also to boot. But this argument ignores a central problem as well. (1/11)

I completely agree that CDSL is a business that produces ample amount of Free Cash. So, it begs the question: "What are they doing with all that cash?" Generally, firms can utilize the cash on their books in 4 ways: Dividends, Acquisitions, Capex/Investments and Buybacks. (2/11)

CDSL does have a Dividend Payout Ratio of ~35-40%. But Dividends are the least efficient way of utilizing cash, due to the Triple Taxation on Dividends. More here:

https://t.co/DZCmOJ0TFi

(3/11)

Handled well, Inorganic Growth is so lucrative that some companies build their business models around acquisitions (Say, MSSL or Cyient). However, CDSL literally CAN'T be one such company. Read 7 (c) of the below regulatory document to know more:

https://t.co/071lwnnwJ4

(4/11)

CDSL can also reinvest cash into their own business, like most companies do. But CDSL (And most Exchanges) have little need for Capex/Reinvestment. CDSL's IPO came in at Rs. 523.99 Crores. Two years in, the Cash and Investments on their books stands at Rs. 650 Crores. (5/11)

In comparison, their Non-Financial Fixed Assets are only Rs. 75 Crores. Most of their cash sits in Debt instruments and Debt MFs. If this is the case, isn't it better to let the shareholders decide what securities they'd rather invest in? (i.e. Pay Dividends instead) (6/11)

That leaves us with Buybacks. If CDSL does a buyback, BSE's stake in CDSL will increase, which cannot cross 24%. Read 2 Para, Page 11 to know more:

https://t.co/ss1bYu5qGM

The recently introduced Buyback Tax is also a bummer, no doubt. (7/11)

If BSE agrees to dilute its stake in CDSL in a periodic manner, CDSL can do Buybacks at the right prices in the future. But this means that BSE shareholders lose out on all that value creation. So, this is an unlikely event too. (8/11)

In conclusion, CDSL IS a cashflow machine, but the uses of the cash are severely restricted. The best way to create shareholder value seems to be Dividends, which is ironically the LEAST efficient way to utilize cash for most firms. (9/11)

If your investment thesis for CDSL is anything other than a slow-to-moderate grower, with stable Margins and a buttload of Dividends, then you need to wake up and smell the salt. (10/11)

ANY investment can be great, when the right price is paid. If you'd like to know my opinion on how much CDSL is worth, visit the blog post below. I discuss the above points and more, converting the theory into numbers used in a Valuation model:

https://t.co/nhcpvkllMS

(11/11)