FIRST LIGHT

01 February 2020

RESEARCH

BOB Economics Research | Economic Survey 2019-20

Pro-Growth

BOB Economics Research | 1st RE of National Income

FY19 growth revised to 6.1%

State Bank of India | Target: Rs 400 | +26% | BUY

Recoveries aid earnings growth

Tech Mahindra | Target: Rs 840 | +5% | REDUCE

Good quarter buoyed by communications vertical

Indian Oil Corp | Target: Rs 200 | +76% | BUY

Uncertainties abound but look priced in

Laurus Labs | Target: Rs 510 | +17% | BUY

Another good beat – TP raised to Rs 510

SUMMARY

India Economics: Economic Survey 2019-20

Economic Survey estimates growth to improve to 6-6.5% in FY21 from 5% in FY20 on the back of a low base, higher global demand and measures taken by the government to improve investment and consumption. The Survey postulates a larger role for private sector and entrepreneurs to achieve US$ 5tn economy by 2025. It also highlights the need to improve India's ranking in enforcing contracts and starting a business as entrepreneurship and growth are inter-related. We believe the Budget will focus on introducing legislations which enable the same.

Click here for the full report.

TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Bajaj Finance	Buy	5,200
Cipla	Buy	570
Eicher Motors	Buy	25,000
Petronet LNG	Buy	400
Reliance Industries	Buy	1,860

MID-CAP IDEAS

Company	Rating	Target
Alkem Labs	Buy	2,290
Future Supply	Buy	680
Greenply Industries	Buy	210
Laurus Labs	Buy	510
Ashok Leyland	Sell	68

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.59	0bps	(29bps)	(104bps)
India 10Y yield (%)	6.56	(2bps)	1bps	(73bps)
USD/INR	71.49	(0.3)	(0.2)	(0.6)
Brent Crude (US$/bbl)	58.29	(2.5)	(14.8)	(5.8)
Dow	28,859	0.4	1.4	15.4
Shanghai	2,977	(2.8)	(2.1)	15.2
Sensex	40,914	(0.7)	(1.6)	12.8
India FII (US$ mn)	**29 Jan**	**MTD**	**CYTD**	**FYTD**
FII-D	41.2	(1,596.7)	(1,596.7)	1,347.4
FII-E	(202.6)	1,897.0	1,897.0	9,286.2

Source: Bank of Baroda Economics Research

BOBCAPS Research
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India Economics: 1st RE of National Income

CSO has revised FY18 and FY19 GDP growth lower by 20bps and 70bps respectively. The downward revision in FY18 is led by public (7.8% lower than earlier) and private (8.9% lower) investment and in FY19 by private consumption (1.1% lower). Household real estate demand seems to be holding up. Financial savings have fallen to 6.5% of GDP in FY19 (7.7% in FY18). The dip in investments and household financial savings calls for policy response through higher government spending and incentivising financial savings.

Click here for the full report.

State Bank of India

State Bank of India's (SBIN) Q3FY20 PAT at Rs 56bn was driven by strong NII growth and lower provisions, but a one-time DTA charge shaved Rs 13bn off earnings. Asset quality improved despite higher slippages, with GNPA/ NNPA declining 25bps/14bps QoQ to 6.9%/2.7%. The SMA book declined to Rs 81bn vs. Rs 183bn in Q2 due to upgrades and recoveries. Fresh slippages were higher at Rs 165bn largely due to DHFL exposure. We broadly maintain estimates and roll forward to a revised Mar'21 TP of Rs 400 (vs. Rs 360).

Click here for the full report.

Tech Mahindra

Tech Mahindra's (TECHM) swift ramp-up of the AT&T deal aided a Q3 revenue beat (up 4.3% QoQ CC to US$ 1.4bn vs. 3% estimated). EBITDA margins at 16.2% (–40bps QoQ) were weighed down by higher subcontracting expenses. A US$ 900mn deal from Jackson Life Insurance lifted Q3 deal TCV to US$ 1.2bn. Management is targeting above-industry growth in the enterprise business and steady growth in communications. We increase FY21/FY22 EPS by 7%/6% and roll to a Mar'21 TP of Rs 840 (from Rs 740).

Click here for the full report.

Indian Oil Corporation

IOCL's Q3FY20 EBITDA at Rs 66bn (+84% YoY) was well above estimates. Key highlights: (a) adj. GRM outperformed at US$ 2.2/bbl, (b) adj. marketing business EBITDA also beat estimates at Rs 40.4bn (Rs 1,670/mt), (c) pipeline/petrochemicals EBITDA trends were mixed at Rs 15.5bn/Rs 7.4bn. We lower FY20/FY21/FY22 earnings by 23%/13%/13% as we cut GRM estimates by US$ 1/bbl given that the anticipated gains from IMO remain elusive. Rolling valuations forward, we have a Mar'21 TP of Rs 200 (from Rs 240).

Click here for the full report.

Laurus Labs

Laurus Labs reported a consecutive beat with best-ever Q3 EBITDA, led by strong operating leverage in formulations and higher gross margins. Weakness in ARVs and Onco API was a key negative. EBITDA stood at Rs 1.5bn with 20.3% margins. PAT was at Rs 736mn due to low tax. Laurus expects to sustain the momentum in coming quarters. New formulation capacity by Apr-Jun'20 should drive 20% growth in FY21. Improving return ratios and positive FCF are focus areas. We raise FY21/FY22 EBITDA 3-5% and our TP 6% to Rs 510.

Click here for the full report.

ECONOMIC SURVEY 2019-20

31 January 2020

Pro-Growth

Sameer Narang
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Economic Survey estimates growth to improve to 6-6.5% in FY21 from 5% in FY20 on the back of a low base, higher global demand and measures taken by the government to improve investment and consumption. The Survey postulates a larger role for private sector and entrepreneurs to achieve US$ 5tn economy by 2025. It also highlights the need to improve India's ranking in enforcing contracts and starting a business as entrepreneurship and growth are inter-related. We believe the Budget will focus on introducing legislations which enable the same.

KEY HIGHLIGHTS

- Growth is projected at 6-6.5% in FY21.
- Higher private sector participation, entrepreneurship and EODB to drive growth higher.
- Higher exports and participation in the GSC to drive job creation.

Growth estimated at 6-6.5% for FY21: Economic Survey estimates growth to increase from 5% in FY20 to 6-6.5% in FY21 driven by low statistical base and reforms undertaken: corporate tax rate cut, infra pipeline (Rs 102tn), asset monetisation and lower interest rates. Higher global growth in 2020 as well as improvement in foreign investments should result in a pick-up in growth. It also points out that growth is not overstated using cross country comparisons.

Wealth creation through entrepreneurship: The Survey talks about importance and virtue of wealth creation to achieve US$ 5tn economy. It shows the benefit of moving from pro-crony structure to pro-business structure wherein new businesses can drive growth higher. The survey shows that a 10% increase in new firms in a district results in a 1.8% rise in GDDP. Notably, India has seen a sharp increase in new businesses (3rd largest in the world).

Improving ease of doing business: The Survey notes need for improvement in EODB parameters such as starting a business, registering property, paying taxes and enforcing contracts. These areas require greater attention to improve export competitiveness and growth.

Privatisation, the way forward: Survey analysed performance of 11 CPSEs in various segments that had undergone strategic disinvestment from FY00-FY04 and proved to be better in performance of major financial parameters. Thus the Budget is likely to focus on asset monetization to fund infra sector.

Job creation through exports: Following China's lead, India too can improve exports and create more jobs by focusing on specialised labour-intensive products and integration into GSCs. The Survey postulates huge potential for "network products" (US$ 7tn by 2025) which will create 40mn jobs by 2025 and 80mn by 2030 and contribute towards the objective of US$ 5tn economy.

Bank of Baroda

1ST RE OF NATIONAL INCOME

31 January 2020

FY19 growth revised to 6.1%

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CSO has revised FY18 and FY19 GDP growth lower by 20bps and 70bps respectively. The downward revision in FY18 is led by public (7.8% lower than earlier) and private (8.9% lower) investment and in FY19 by private consumption (1.1% lower). Household real estate demand seems to be holding up. Financial savings have fallen to 6.5% of GDP in FY19 (7.7% in FY18). The dip in investments and household financial savings calls for policy response through higher government spending and incentivising financial savings.

Growth estimates for FY18/19 revised downwards: While GDP and GVA growth for FY18 has been revised downwards by 20bps and 30bps respectively, for FY19 GDP and GVA growth has been revised downward by 70bps and 60bps respectively. The downward revision in GVA is attributable to mining and quarrying (now at -5.8% versus 1.3% earlier) as well as manufacturing (now 5.7% versus 6.9% earlier) in FY19. It seems industrial slowdown had started in FY19 itself which is in-line with high frequency indicators.

Public and private investment for FY18 revised lower: While government consumption has been revised upwards by 90bps in FY19, private consumption has been revised downwards by 90bps. For FY18, GFCF has been revised down by 210bps led by private and public investment. Private corporate investment increased by only 2% and public investment by 3.3% compared with earlier estimate of 10.9% and 11.1% respectively. Lower spending by state governments and implementation of GST explain the downward revision to earlier estimates. New estimates show need for further policy intervention.

Savings rate shows moderation: India's savings rate edged down to 30.1% in FY19 from 32.4% in FY18. This was led by moderation in household savings rate to 18.2% compared with 19.2% in FY18. Household financial savings decelerated sharply to 6.5% in FY19 compared with 7.7% in FY18. However, residential investment was higher by 30bps at 11.5%. Private corporate sector too has seen a 1.2% decline in savings rate. Given the sharp deceleration in household financial savings, Budget may look at increasing the current limit for financial savings under Section 80C of the Income Tax Act.

BUY
TP: Rs 400 | 26%

STATE BANK OF INDIA | Banking | 31 January 2020

Recoveries aid earnings growth

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State Bank of India's (SBIN) Q3FY20 PAT at Rs 56bn was driven by strong NII growth and lower provisions, but a one-time DTA charge shaved Rs 13bn off earnings. Asset quality improved despite higher slippages, with GNPA/NNPA declining 25bps/14bps QoQ to 6.9%/2.7%. The SMA book declined to Rs 81bn vs. Rs 183bn in Q2 due to upgrades and recoveries. Fresh slippages were higher at Rs 165bn largely due to DHFL exposure. We broadly maintain estimates and roll forward to a revised Mar'21 TP of Rs 400 (vs. Rs 360).

Asset quality improving directionally: Fresh slippages were higher at Rs 165bn in Q3 (vs. Rs 88bn in Q2) due to DHFL exposure totalling ~Rs 100bn. SBIN has provided 20%/50% on its ~Rs 71bn/~Rs 30bn funded/bond exposure to DHFL (overall PCR of ~30%). Retail/agri/SME slippages were largely steady QoQ. The bank had interest income/provision reversals worth Rs 40bn/Rs 78bn on recovery of stressed assets. Recoveries are expected from three accounts via resolution in Q4 – Bhushan Power (Rs 40bn), the textile sector (Rs 20bn) and power sector (Rs 10bn). SBIN has restructured ~70k eligible accounts worth Rs 36bn under the RBI's MSME scheme (~50% restructured in Q3).

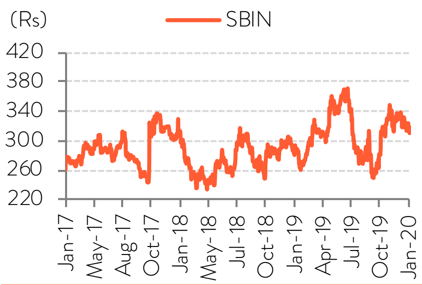
Corporate book drags down loan growth: Loan growth at 7% YoY was marred by weak corporate account growth due to low working capital utilisation levels. Retail loan growth remained strong at 17% while the international book grew 16% YoY. Domestic NIM at 3.27% has largely peaked as there is no large recovery in sight, while interest rates on deposits have bottomed. Improvement, if any, should come from a better portfolio mix and increase in loans accruing interest.

Maintain BUY: We view SBIN as one of the prime beneficiaries of the revival in corporate loan cycle. Maintain BUY with our TP revised to Rs 400 on rollover.

Ticker/Price	SBIN IN/Rs 318
Market cap	US$ 39.8bn
Shares o/s	8,925mn
3M ADV	US$ 159.7mn
52wk high/low	Rs 374/Rs 244
Promoter/FPI/DII	59%/9%/32%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Net interest income	748,537	883,489	1,004,362	1,176,621	1,401,398
NII growth (%)	21.0	18.0	13.7	17.2	19.1
Adj. net profit (Rs mn)	(65,474)	8,622	303,684	359,511	424,900
EPS (Rs)	(7.7)	1.0	34.0	40.3	47.6
P/E (x)	(41.1)	329.6	9.4	7.9	6.7
P/BV (x)	1.3	1.3	1.1	1.0	0.9
ROA (%)	(0.2)	0.0	0.8	0.8	0.9
ROE (%)	(3.2)	0.4	12.6	13.1	14.0

Source: Company, BOBCAPS Research

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REDUCE
TP: Rs 840 | ⮝ 5%

TECH MAHINDRA | IT Services | 31 January 2020

Good quarter buoyed by communications vertical

Tech Mahindra's (TECHM) swift ramp-up of the AT&T deal aided a Q3 revenue beat (up 4.3% QoQ CC to US$ 1.4bn vs. 3% estimated). EBITDA margins at 16.2% (–40bps QoQ) were weighed down by higher subcontracting expenses. A US$ 900mn deal from Jackson Life Insurance lifted Q3 deal TCV to US$ 1.2bn. Management is targeting above-industry growth in the enterprise business and steady growth in communications. We increase FY21/FY22 EPS by 7%/6% and roll to a Mar'21 TP of Rs 840 (from Rs 740).

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Upbeat revenue...: Revenue at US$ 1.4bn increased 4.3% QoQ CC, ahead of our/street estimates of 3%/2.2% growth. However, EBITDA margins at 16.2% slipped 40bps QoQ, coming in below our estimate due to higher subcontracting expenses (at 16.3% of revenues vs. 15.1% in Q2) in an otherwise efficient quarter. Utilisation increased 200bps QoQ with a largely stable onsite/offshore revenue mix.

...led by faster-than-expected AT&T deal transition: The communications vertical led revenue growth at 8.9% QoQ in dollar terms, followed by retail, transport and logistics (+8.1% QoQ) and BFSI (+6.7%QoQ). Enterprise business grew 2.4% QoQ in dollar terms.

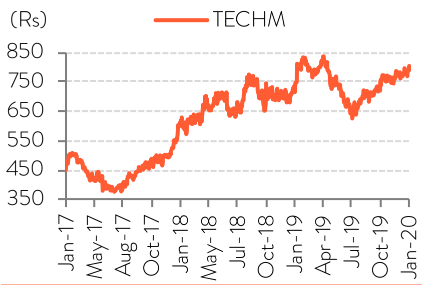
Skewed performance at top clients: Top 5 client revenue increased 8.5% QoQ in dollar terms, likely aided by ramp-up of the AT&T deal. On the other hand, top 6 to 20 client revenue declined by 5.4% QoQ.

Healthy deal wins: New contract signings worth US$ 1.2bn marked the second consecutive quarter of US$ 1bn+ deal TCV. A US$ 900mn TCV award from Jackson Life Insurance supported healthy deal wins in Q3.

Ticker/Price	TECHM IN/Rs 797
Market cap	US$ 9.7bn
Shares o/s	873mn
3M ADV	US$ 23.8mn
52wk high/low	Rs 847/Rs 607
Promoter/FPI/DII	36%/39%/25%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	3,07,729	3,47,421	3,70,511	4,10,889	4,54,685
EBITDA (Rs mn)	47,169	63,368	61,195	72,717	84,300
Adj. net profit (Rs mn)	38,001	42,975	44,071	49,601	56,318
Adj. EPS (Rs)	42.7	47.7	50.1	56.4	64.0
Adj. EPS growth (%)	33.6	11.9	5.0	12.5	13.5
Adj. ROAE (%)	21.0	21.4	20.0	20.1	20.3
Adj. P/E (x)	18.7	16.7	15.9	14.1	12.4
EV/EBITDA (x)	14.3	10.9	11.3	9.3	7.6

Source: Company, BOBCAPS Research

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BUY
TP: Rs 200 | ⮝ 76%

INDIAN OIL CORP | Oil & Gas | 31 January 2020

Uncertainties abound but look priced in

IOCL's Q3FY20 EBITDA at Rs 66bn (+84% YoY) was well above estimates. Key highlights: (a) adj. GRM outperformed at US$ 2.2/bbl, (b) adj. marketing business EBITDA also beat estimates at Rs 40.4bn (Rs 1,670/mt), (c) pipeline/petrochemicals EBITDA trends were mixed at Rs 15.5bn/Rs 7.4bn. We lower FY20/FY21/FY22 earnings by 23%/13%/13% as we cut GRM estimates by US$ 1/bbl given that the anticipated gains from IMO remain elusive. Rolling valuations forward, we have a Mar'21 TP of Rs 200 (from Rs 240).

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GRMs outperform but trend remains weak: IOCL's GRMs (at US$ 2.2/bbl) outperformed the Singapore benchmark (US$ 1.7/bbl) in Q3FY20. A relatively high diesel slate in the refining portfolio puts the company in an advantageous position, given that the new IMO regulations (effective Jan'20) that are expected to push diesel spreads above US$ 20/bbl (from ~US$ 13 currently). Paradip refinery GRMs remain a key factor behind IOCL's outperformance.

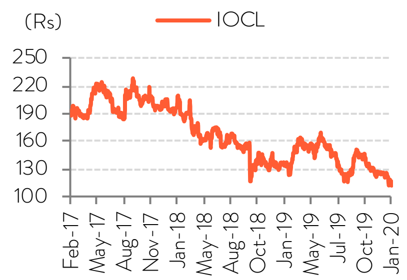
Marketing earnings improve: Marketing business EBITDA at Rs 40bn was in line with estimates as IOCL gained market share in ATF and industrial product sales (while ceding share in bulk diesel and petrol). Pipeline business EBITDA underperformed at Rs 15.5bn (–4% YoY) on lower volumes (21mmt, –9% YoY). Petchem margins beat estimates at US$ 165/MT (–18% YoY), leading to above-expected EBITDA at Rs 7.4bn (–24% YoY). Petchem volumes recovered to 0.63mmt (+20% QoQ) and could improve further on commissioning of the new PP plant in Paradip.

Valuations building in the worst case: At 4.7x FY22E EBITDA, valuations seem to be pricing in the worst case (i.e. possibility of a BPCL acquisition or GRMs sustaining at <US$ 3/bbl). Reiterate BUY.

Ticker/Price	IOCL IN/Rs 113
Market cap	US$ 15.4bn
Shares o/s	9,712mn
3M ADV	US$ 25.0mn
52wk high/low	Rs 171/Rs 112
Promoter/FPI/DII	52%/8%/41%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	4,214,918	5,281,489	5,578,406	6,675,351	7,287,866
EBITDA (Rs mn)	416,275	352,227	298,235	391,763	425,787
Adj. net profit (Rs mn)	221,911	173,837	144,655	189,288	205,184
Adj. EPS (Rs)	23.4	18.9	15.8	20.6	22.3
Adj. EPS growth (%)	11.7	(19.1)	(16.8)	30.9	8.4
Adj. ROAE (%)	20.6	15.4	12.8	16.3	16.7
Adj. P/E (x)	4.8	6.0	7.2	5.5	5.1
EV/EBITDA (x)	4.1	4.9	6.3	5.1	4.7

Source: Company, BOBCAPS Research

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BUY
TP: Rs 510 | 17%

LAURUS LABS | Pharmaceuticals | 31 January 2020

Another good beat – TP raised to Rs 510

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Laurus Labs reported a consecutive beat with best-ever Q3 EBITDA, led by strong operating leverage in formulations and higher gross margins. Weakness in ARVs and Onco API was a key negative. EBITDA stood at Rs 1.5bn with 20.3% margins. PAT was at Rs 736mn due to low tax. Laurus expects to sustain the momentum in coming quarters. New formulation capacity by Apr-Jun'20 should drive 20% growth in FY21. Improving return ratios and positive FCF are focus areas. We raise FY21/FY22 EBITDA 3-5% and our TP 6% to Rs 510.

Best-ever EBITDA and margin beat look sustainable: Sequentially, the quarter saw a strong sales pickup in high-margin business (ex-ARV) from 51% to 68% share. Formulation sales came in at US$ 40mn vs. estimates of US$ 25mn. Other API segment grew 99% YoY (14% QoQ) led by CVS, driving gross margins of 50.6% (11-quarter high) and EBITDA margins of 20.3% (+380bps YoY, 96bps QoQ). The margin beat could sustain led by a good LMIC order book, TLE400/600mg and TEE approvals in H1FY21. Management is bullish on the non-Aspen CDMO business and expects >20% growth in FY20-FY23.

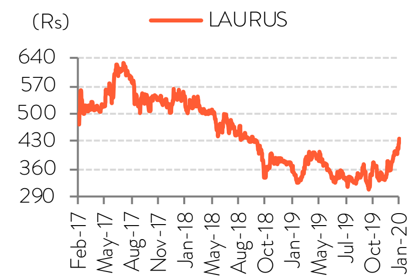
Solid execution on formulations: Formulations clocked >25% EBITDA margins for 9MFY20 (assuming 50% gross margin and US$ 20mn opex as per management). Laurus has raised the FY20 sales target from US$ 70mn to US$ 120mn and expects 20% growth in FY21 as debottlenecked capacity will be available by Apr-Jun'20, leading to upward revision in our estimates.

Earnings call highlights: (1) RM price disruption from the coronavirus outbreak not visible as of now but can have an impact if operational shutdown continues beyond March. (2) ARV sales to recover in FY21 – Q3 weakness due to delay in supplementary tender. (3) 9M capex at Rs 1.4bn (vs. Rs 2.5bn guided for FY21).

Ticker/Price	LAURUS IN/Rs 436
Market cap	US$ 648.7mn
Shares o/s	106mn
3M ADV	US$ 0.8mn
52wk high/low	Rs 443/Rs 303
Promoter/FPI/DII	33%/9%/39%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	20,562	22,919	27,500	31,873	35,731
EBITDA (Rs mn)	4,134	3,560	5,080	6,531	7,617
Adj. net profit (Rs mn)	1,483	937	1,650	2,663	3,266
Adj. EPS (Rs)	13.9	8.8	15.5	25.0	30.7
Adj. EPS growth (%)	(10.8)	(36.8)	76.0	61.4	22.6
Adj. ROAE (%)	10.5	6.2	10.1	14.6	15.5
Adj. P/E (x)	31.3	49.5	28.1	17.4	14.2
EV/EBITDA (x)	13.6	15.8	11.2	8.8	7.5

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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