FIRST LIGHT

12 November 2021

RESEARCH

Pidilite Industries | Target: Rs 2,080 | –16% | SELL

Broad-based growth but sharp RM headwinds a drag

CESC | Target: Rs 91 | –0% | HOLD

Fairly priced but upside if distribution is delicensed

Tech Mahindra | Target: Rs 1,890 | +24% | BUY

Positive commentary instils confidence; 5G outlook optimistic

SUMMARY

Pidilite Industries

- Consolidated Q2 net revenue up 40% YoY to Rs 26.3bn. Like-to-like growth at 33% (ex-PAPL)
- Gross margin contracted 1,050bps YoY to 45.4% on account of sharp increase in VAM price to US$ 2,071/mt vs. US$ 765/mt
- Target multiple raised given growth traction but RM headwinds prompt earnings cut. Retain SELL; new Sep'22 TP at Rs 2,080 (vs. Rs 1,525)

Click here for the full report.

CESC

- Despite steady 8% YoY growth in Q2 pretax income, consolidated net income fell 11% due to lower tax rate in comparable quarter
- Distribution delicensing could open up large market for CESC – one of the few experienced players in this space
- Raise TP to Rs 91 (vs. Rs 75) on higher net income estimates but retain HOLD as current valuations capture business prospects

Click here for the full report.

Daily macro indicators

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.55	11bps	(6bps)	57bps
India 10Y yield (%)	6.34	4bps	2bps	43bps
USD/INR	74.38	(0.5)	0.8	0.0
Brent Crude (US$/bbl)	82.64	(2.5)	0.3	88.7
Dow	36,080	(0.7)	3.8	22.7
Shanghai	3,492	(0.4)	(2.8)	4.5
Sensex	60,353	(0.1)	0.5	38.4
India FII (US$ mn)	**09-Nov**	**MTD**	**CYTD**	**FYTD**
FII-D	(46.3)	(55.7)	(126.1)	1,901.2
FII-E	85.5	(5.6)	6,253.0	(1,073.3)

Source: Bloomberg

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Tech Mahindra

- TECHM's analyst meet today focused on the 3Ps – Purpose, People and Performance
- Management aims to raise the revenue run-rate of most verticals to US$ 1bn in two years. CME will remain the key focus vertical
- We stay positive on TECHM post encouraging commentary on revenue growth, 5G traction, margins and M&A – restate BUY, TP Rs 1,890

Click here for the full report.

RESULT REVIEW

SELL

TP: Rs 2,080 | ∨ 16%

PIDILITE INDUSTRIES | Construction Materials | 12 November 2021

Broad-based growth but sharp RM headwinds a drag

- **Consolidated Q2 net revenue up 40% YoY to Rs 26.3bn. Like-to-like growth at 33% (ex-PAPL)**
- **Gross margin contracted 1,050bps YoY to 45.4% on account of sharp increase in VAM price to US$ 2,071/mt vs. US$ 765/mt**
- **Target multiple raised given growth traction but RM headwinds prompt earnings cut. Retain SELL; new Sep'22 TP at Rs 2,080 (vs. Rs 1,525)**

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Broad-based revenue growth: PIDI's consolidated Q2FY22 net revenue grew 40% YoY to Rs 26.3bn (33% on like-to-like basis which excludes PAPL). Consumer & Bazaar (C&B) segment revenue increased 40% YoY to Rs 21.3bn but segmental EBIT margin declined 750bps to 27.4%. The B2B segment grew 41% YoY to Rs 5.3bn with EBIT margin down 275bps YoY to 5%.

Strong RM headwinds: Gross margin contracted 1,050bps YoY (-370bps QoQ) as prices of key material VAM increased to US$ 2,071/mt vs. US$ 765/mt in Q2FY21 (US$ 1,610/mt in Q1). A decline in employee cost/other expenses as a percentage of sales (-250bps/-170bps YoY) limited EBITDA margin contraction at 630bps YoY to 20.9%. EBITDA grew 7% YoY to Rs 5.5bn.

Standalone performance: Sales volume and mix growth stood at 25% YoY, with 25%/20% growth in C&B/B2B. Net sales grew 36% YoY to Rs 22.1bn. C&B revenue rose 35% YoY to Rs 18bn while EBIT margin contracted 825bps to 28.5%. B2B revenue grew 40% YoY to Rs 4.4bn with a 420bps margin decline to 9.7%. Gross/EBITDA margin contracted by 1,100bps/730bps YoY to 45.5%/21.6%.

Estimates trimmed: While PIDI has delivered strong, broad-based sales and earnings growth, we prune FY22/FY23 EPS estimates by 10%/3% given rising VAM prices (up from US$ 2,071/mt in Q2 to spot levels of US$ 2,300-2,400/mt). We expect spiraling input costs to sustain/peak in the near term leading to stressed margins. While PIDI has initiated calibrated price hikes during the quarter, these cover only ~75% of inflation. Management is consciously looking to absorb the partial impact given high volatility in input prices and near-term demand uncertainty.

Valuations stretched; maintain SELL: We remain positive on PIDI's long-term story given its strong presence in waterproofing and construction chemicals (first-mover advantage) and robust connect with trade channels. However, the stock looks overvalued at current levels of 78x FY23E EPS. We roll forward to a revised Sep'22 TP of Rs 2,080 (Rs 1,525 earlier), based on a 60x one-year forward P/E multiple (45x earlier), in line with the five-year median. SELL.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	PIDI IN/Rs 2,474
Market cap	US$ 16.9bn
Free float	30%
3M ADV	US$ 14.6mn
52wk high/low	Rs 2,532/Rs 1,501
Promoter/FPI/DII	70%/12%/18%

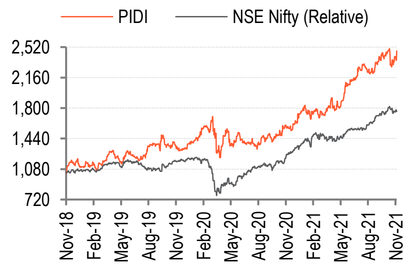
Source: NSE | Price as of 11 Nov 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	72,927	89,662	1,03,920
EBITDA (Rs mn)	16,806	19,008	23,694
Adj. net profit (Rs mn)	11,339	12,773	16,113
Adj. EPS (Rs)	22.3	25.1	31.7
Consensus EPS (Rs)	22.3	26.5	33.1
Adj. ROAE (%)	22.6	21.8	25.0
Adj. P/E (x)	110.9	98.4	78.0
EV/EBITDA (x)	74.6	65.9	52.9
Adj. EPS growth (%)	(2.2)	12.7	26.1

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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HOLD
TP: Rs 91 | ∀ 0%

CESC | Power | 11 November 2021

Fairly priced but upside if distribution is delicensed

- **Despite steady 8% YoY growth in Q2 pretax income, consolidated net income fell 11% due to lower tax rate in comparable quarter**
- **Distribution delicensing could open up large market for CESC – one of the few experienced players in this space**
- **Raise TP to Rs 91 (vs. Rs 75) on higher net income estimates but retain HOLD as current valuations capture business prospects**

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Pretax income up 8% YoY: CESC reported a Q2FY22 consolidated net income decline of 11% YoY due to a 146% increase in taxation from a higher effective tax rate (29%) versus a low base (13%). Note that the tax rate in regulated utilities can be volatile. Pretax income was up 8% YoY driven by a drop in interest cost and higher other income. Sequentially, net income rose 24% QoQ due to an 11% increase in EBIT and a 54% increase in other financial income.

Well positioned to benefit from opening up of electricity distribution: CESC is India's fourth largest private electricity distributor with ~1% volume share and decades of experience in supplying electricity to the city of Kolkata under the regulated return model and to Greater Noida, besides franchisee assets. The company has won the concession for power distribution in Chandigarh. Delicensing of distribution through the Electricity (Amendment) Bill 2021 will open up a huge opportunity to offer services pan India which will benefit CESC as it is among a handful of private companies engaged in distribution.

Estimates raised by 7-9%: We raise our FY22/FY23/FY24 net income estimates by 7%/7%/9% to factor in lower AT&C loss assumptions in franchisee distribution circles and reduced interest rates. We have also stripped the renewables business from our estimates following its sale to Torrent Power and excluded Chandigarh distribution as it has not been formally transferred to the company.

Retain HOLD, change TP to Rs 91: We raise our SOTP-based Sep'22 TP to Rs 91 from Rs 75 led by our higher PAT estimates and lower interest rate assumptions which reduce the WACC used to value CESC's different businesses. Our TP implies an FY22E EV/EBITDA of 6.1x, close to the 10-year mean. We retain HOLD as we believe that the current business prospects are already captured in the price. Passage of the Electricity Act could, however, raise growth prospects and, therefore, valuations. New distribution wins would act as another positive stock driver.

Key changes

Target	Rating
▲	◄ ►

Ticker/Price	CESC IN/Rs 91
Market cap	US$ 1.6bn
Free float	48%
3M ADV	US$ 5.5mn
52wk high/low	Rs 102/Rs 56
Promoter/FPI/DII	52%/13%/23%

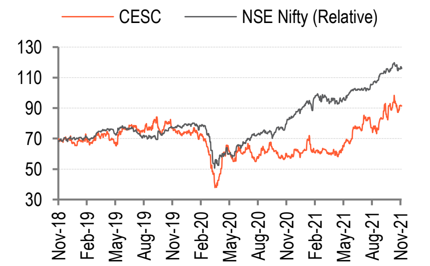
Source: NSE | Price as of 11 Nov 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	1,16,390	1,31,525	1,34,804
EBITDA (Rs mn)	36,100	35,762	35,998
Adj. net profit (Rs mn)	13,310	14,733	15,611
Adj. EPS (Rs)	10.0	11.1	11.8
Consensus EPS (Rs)	10.0	10.6	11.7
Adj. ROAE (%)	13.7	14.3	14.0
Adj. P/E (x)	9.1	8.2	7.8
EV/EBITDA (x)	6.6	6.4	6.2
Adj. EPS growth (%)	(89.8)	10.7	6.0

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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BUY
TP: Rs 1,890 | ⮝ 24%

TECH MAHINDRA | Technology & Internet | 12 November 2021

Positive commentary instils confidence; 5G outlook optimistic

- **TECHM's analyst meet today focused on the 3Ps – Purpose, People and Performance**
- **Management aims to raise the revenue run-rate of most verticals to US$ 1bn in two years. CME will remain the key focus vertical**
- **We stay positive on TECHM post encouraging commentary on revenue growth, 5G traction, margins and M&A – restate BUY, TP Rs 1,890**

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We attended TECHM's analyst day. Key takeaways from the event:

Unlocking M&A synergies: TECHM will continue to undertake more M&A as this is not only a source of revenue and helps to enrich white spaces in its capability, but is also an important part of talent development (for recruiting senior leaders). The company has won US$ 700mn in large deals led by portfolio company synergies in FY22TD. The synergy-led pipeline is now at US$ 1.3bn. The large healthcare deal won in Q2FY22 was made possible by combining the capabilities of portfolio assets.

Billion-dollar target for technology & healthcare verticals: TECHM counts on its billion-dollar client club to spur enterprise business growth, where management is targeting US$ 1bn+ in revenue each from the hi-tech/technology and healthcare (HLS) verticals (vs. respective Q2FY22 annualised run-rates of US$ 530mn and US$ 400mn).

In BFSI, it is aiming for a US$ 1.5bn run-rate over the next one year. CME (communications, media & entertainment) remains the key growth driver for the foreseeable future with HLS and technology as the 'growth gem' verticals (i.e. TECHM will make extraordinary efforts to accelerate their growth). Some of the largest deal wins are in HLS. Hi-tech is also expected to show similar momentum.

5G update: Management expects 5G to contribute US$ 3.7tn to the global economy by 2030. 5G constituted 20% of TECHM's telecom revenue and 50% of network revenue in Q2FY22, crossing US$ 500mn. It is expected to fuel growth in the CME vertical which was up 16% YoY in Q2FY22. TECHM's 5G strategy is built around (1) modernising infrastructure, (2) digitising products and platforms, (3) monetising the data and business, and (4) reimagining customer experience. 5G revenue streams will come from enterprises, ecosystems and devices. Please see our Deep Dive report of 14 Sep 2021: **5G juggernaut gains momentum; BUY TECHM.**

Positive on TECHM: Our positive view is reinforced by management's upbeat outlook on large deals, margins, revenue growth, M&A and deal pricing. We retain BUY with an unchanged Sep'22 TP of Rs 1,890, based on 22.5x one-year forward P/E.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	TECHM IN/Rs 1,522
Market cap	US$ 17.8bn
Free float	64%
3M ADV	US$ 69.8mn
52wk high/low	Rs 1,630/Rs 820
Promoter/FPI/DII	36%/39%/25%

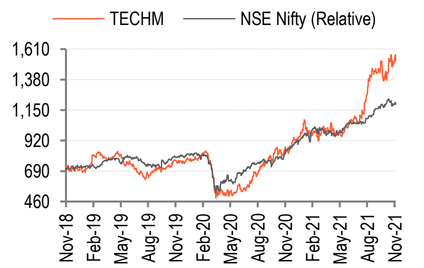
Source: NSE | Price as of 11 Nov 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	378,551	441,203	516,470
EBITDA (Rs mn)	68,471	82,513	102,807
Adj. net profit (Rs mn)	44,281	57,302	70,359
Adj. EPS (Rs)	50.4	65.2	80.0
Consensus EPS (Rs)	50.4	63.9	72.7
Adj. ROAE (%)	18.7	21.4	23.3
Adj. P/E (x)	30.2	23.4	19.0
EV/EBITDA (x)	19.3	16.0	12.7
Adj. EPS growth (%)	4.2	29.4	22.8

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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