FIRST LIGHT

16 July 2021

RESEARCH

[Sector Report] Logistics

Structural drivers yet to take root; prefer MAHLOG, VRLL

Wipro | Target: Rs 590 | +2% | HOLD

Simplified operating model pays off

SUMMARY

Logistics

- Structural growth drivers such as shift to organised players, outsourcing/3PL and manufacturing scale-up are yet to materialise
- Cyclical recovery has begun post second Covid wave with new manufacturing orders, recovering auto sales and strong trade data
- Retain MAHLOG and VRLL at BUY on high recovery-led growth prospects. TCIEXP and TRPC cut to HOLD after +30% rally; retain CCRI at SELL

Click here for the full report.

Wipro

- WPRO posted an upbeat QoQ performance in Q1FY22 with 12% CC revenue growth, ahead of our (8.9%) and street estimates
- EBIT margin at 19% beat estimates despite sector-wide supply constraints, owing to better margin execution at Capco
- We raise target P/E to 21.7x on strong guidance, roll to a Jun'22 TP of Rs 590 (vs. Rs 470) and realign to HOLD (vs. ADD) per our new rating scale

Click here for the full report.

Daily macro indicators

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.35	(7bps)	(11bps)	72bps
India 10Y yield (%)	6.20	0bps	19bps	39bps
USD/INR	74.59	(0.1)	(2.1)	0.7
Brent Crude (US$/bbl)	74.76	(2.3)	2.8	70.7
Dow	34,933	0.1	1.3	30.0
Shanghai	3,529	(1.1)	(1.7)	5.0
Sensex	52,904	0.3	0.8	46.7
India FII (US$ mn)	**13-Jul**	**MTD**	**CYTD**	**FYTD**
FII-D	64.8	(8.1)	(3,174.9)	(1,147.7)
FII-E	9.4	(340.9)	7,743.2	416.9

Source: Bank of Baroda Economics Research

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LOGISTICS

15 July 2021

Structural drivers yet to take root

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Sector has underperformed: At 5.8% over FY16-FY21, the revenue CAGR of India's top 10 logistics players is below the 6.7% growth clocked by the country's top 1000 listed companies. In our view, listed logistics players are dependent on client segments such as auto, FMCG and engineering which form a small portion of overall logistics spend and have been slow to grow in recent years. In addition, structural drivers are yet to kick in. As a result, the sector has lagged the Nifty in 11 of the last 16 quarters.

Structural drivers yet to take root…: The anticipated shift to the organised sector post GST and Covid-19 has been slow but should accelerate as customer industries become formalised and GST compliance remains a challenge for unorganised players. Outsourcing of logistics (3PL) is stuck at 3% of the market versus the global average of 10% as the formulation of a follow-up roadmap post GST is progressing at a sluggish pace after decades of having a state rather than nationwide plan. Scale in manufacturing/warehousing leading to more distance per tonne will also take time.

...but cyclical recovery underway: Various macro indicators reflect the onset of a post Covid recovery. New order data suggests that manufacturing PMI, albeit still in contraction mode, is likely to improve. Auto, a key logistics customer segment, also saw sales soar in June. Merchandise trade has held up well and rail movement of industrial commodities and container traffic has remained stable. After slipping in May, road traffic is improving with e-way bill and Fastag toll collections up MoM in June.

Recovery priced in; stock selection key: Multiples are close to peaks and on reverse DCF, 3 of our 5 coverage stocks are implying a 10-year FCF CAGR of +20% above the historical mean. Being selective is thus critical. We prefer Mahindra Logistics (MAHLOG, BUY, TP Rs 701) and VRL Logistics (VRLL, BUY, TP Rs 381) as they are most sensitive to market revival and should clock respective FY21-FY23 EPS CAGR of 106% and 72%. MAHLOG is also the most capital efficient and VRLL is the cheapest stock in the sector.

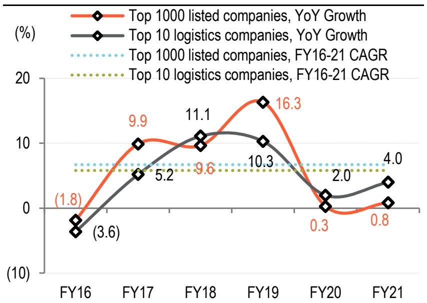
We like TCI Express' (TCIEXP) efficient business model but downgrade it from BUY to HOLD (TP Rs 1,421) as valuations have peaked after a +35% rally post the FY21 results. We similarly downgrade Transport Corp (TRPC, TP Rs 431) after its +30% rally. Retain SELL on Container Corp (CCRI, Rs 521) which remains overvalued.

Recommendation snapshot

Ticker	Price	Target	Rating
CCRI IN	676	521	SELL
MAHLOG IN	583	701	BUY
TRPC IN	400	431	HOLD
TCIEXP IN	1,475	1,421	HOLD
VRLL IN	316	381	BUY

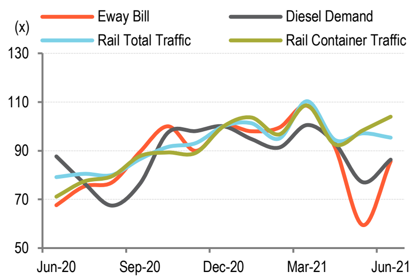
Price & Target in Rupees | Price as of 14 Jul 2021

Growth still cyclical not structural



Source: BOBCAPS Research, Bloomberg

Indicators (Dec'20 = 100) recovering after dip in May



Source: BOBCAPS Research, Bloomberg

HOLD
TP: Rs 590 | 2%

WIPRO | IT Services | 16 July 2021

Simplified operating model pays off

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- **EBIT margin at 19% beat estimates despite sector-wide supply constraints, owing to better margin execution at Capco**
- **We raise target P/E to 21.7x on strong guidance, roll to a Jun'22 TP of Rs 590 (vs. Rs 470) and realign to HOLD (vs. ADD) per our new rating scale**

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All-round outperformance: WPRO reported 12.2% USD QoQ revenue growth in Q1 vs. our estimate of 9.1% USD/8.9% CC. Organic growth of 4.9% CC was the highest in the last 38 quarters, outperforming the guided range of 2-4% QoQ CC. Growth was helmed by BFSI/global media & telecom/retail at 22.8%/14.4%/14.2% QoQ USD. The technology and manufacturing-hi-tech verticals remained weak with flattish growth. BFSI was especially strong due to the Capco acquisition.

EBIT margin at 19% was well ahead of our estimate of 17.9%. This was possible because of better margin execution at Capco (18.8% vs. 17.5% expected). TCV (consisting 8 large deals) was reported at US$ 715mn (vs. US$ 1.4bn in Q4), of which a significant portion represents net new contracts.

Robust outlook: WPRO has guided for 5-7% QoQ CC growth in Q2FY22 (which includes 2-3% growth from the Capco acquisition) on a strong base of Q1. For FY22, management is confident of achieving comfortable double-digit growth, ex-Capco.

Strong new client addition: The company reported 129 new customers during Q1 – its highest ever (contributed partially by Capco). A total of 35/12/16 new clients were added in the US$ 1mn/US$ 3mn/US$ 5mn buckets.

Supply pressure: A record 12,178 employees were added in Q1 (post Capco) indicating sector-wide supply pressure. WPRO is focused on reskilling and increasing hiring to manage the supply crunch. It plans to hire 6,000 freshers in Q2, besides rolling out wage hikes for 80% of its employees during that quarter.

Recommend HOLD: Organisational restructuring has helped WPRO rein in costs despite supply issues. We raise FY22 EPS 16% on higher growth and margin estimates given double-digit organic growth guidance for FY22 and above- expected Capco margins. Recommend HOLD as valuations look stretched.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	WPRO IN/Rs 576
Market cap	US$ 42.7bn
Free float	26%
3M ADV	US$ 78.4mn
52wk high/low	Rs 580/Rs 255
Promoter/FPI/DII	74%/9%/17%

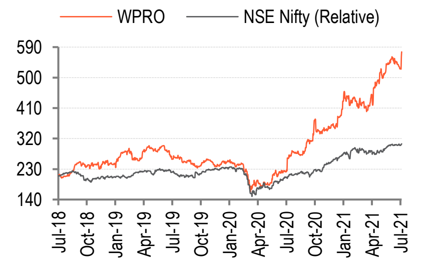
Source: NSE | Price as of 15 Jul 2021

Key financials

Y/E 31 Mar	FY21P	FY22E	FY23E
Total revenue (Rs mn)	622,425	802,859	912,418
EBITDA (Rs mn)	144,560	174,747	204,676
Adj. net profit (Rs mn)	108,783	129,858	149,502
Adj. EPS (Rs)	19.7	23.5	27.1
Consensus EPS (Rs)	19.7	20.9	23.3
Adj. ROAE (%)	19.5	21.2	21.7
Adj. P/E (x)	29.2	24.5	21.3
EV/EBITDA (x)	21.6	17.8	15.1
Adj. EPS growth (%)	18.1	19.4	15.1

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE

Disclaimer

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

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

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