# FIRST LIGHT

12 April 2021

## RESEARCH

### [Sector Report] Internet Technology

Zomato – Leading Indian foodtech play

### BOB Economics Research | Monthly Chartbook

Second wave poses risk to recovery

### Automobiles | Q4FY21 Preview

Margins to remain under pressure

## SUMMARY

### Internet Technology

Zomato's latest pre-IPO funding round elevates its valuation to US$ 5.4bn vs. US$ 3.9bn in Dec'20, on the back of (1) recovery from the initial Covid-led volume slump, (2) improving unit economics, and (3) successful listing of US counterpart DoorDash. Despite DoorDash's stronger annual revenue and margins, we believe Zomato's valuation is justified given potential demand scalability in India's growing, duopolistic market. INFOE which holds 18.4% stake (new Zomato-led TP of Rs 2,780 vs. Rs 2,680) remains a SELL because of weakness in its core businesses.

Click here **for the full report.**

### India Economics: Monthly Chartbook

Rising Covid-19 infections in India pose a risk to our growth estimate of 11.5% in FY22. As of now, at least seven state governments have imposed some form of restrictions to contain infections. However, consumption led recovery currently underway as seen in higher rural demand and imports, have not been impacted. Tax collections—direct and indirect—have also seen a positive surprise. This along with RBI's GSAP 1.0 program for purchase of Rs 1tn of government securities in Q1 has driven domestic yields lower. But RBI's (5%) and our inflation forecast (4.8%) remains above MPC's target of 4%. This implies India's monetary cycle should see normalisation beginning in H2FY22 with 50bps of repo rate hike in FY23.

Click here **for the full report.**

## TOP PICKS

### LARGE-CAP IDEAS

| Company | Rating | Target |
|---|---|---|
| Cipla | Buy | 1,000 |
| TCS | Buy | 3,710 |
| Tech Mahindra | Buy | 1,130 |

### MID-CAP IDEAS

| Company | Rating | Target |
|---|---|---|
| Alkem Labs | Buy | 3,750 |
| Greenply Industries | Buy | 195 |
| Laurus Labs | Buy | 480 |
| Transport Corp | Buy | 330 |

Source: BOBCAPS Research

### DAILY MACRO INDICATORS

| Indicator | Current | 2D (%) | 1M (%) | 12M (%) |
|---|---|---|---|---|
| US 10Y yield (%) | 1.62 | (5bps) | 3bps | 90bps |
| India 10Y yield (%) | 6.03 | (5bps) | (19bps) | (46bps) |
| USD/INR | 74.58 | 0 | (1.8) | 2.2 |
| Brent Crude (US$/bbl) | 63.20 | 0.1 | (7.4) | 100.8 |
| Dow | 33,504 | 0.2 | 5.3 | 41.2 |
| Shanghai | 3,483 | 0.1 | 1.8 | 23.2 |
| Sensex | 49,746 | 0.2 | (1.4) | 59.6 |
| **India FII (US$ mn)** | **7 Apr** | **MTD** | **CYTD** | **FYTD** |
| FII-D | (9.5) | (324.7) | (2,351.9) | (324.7) |
| FII-E | 54.3 | (154.6) | 7,171.7 | (154.6) |

Source: Bank of Baroda Economics Research

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## Automobiles: Q4FY21 Preview

We expect a mixed revenue performance from our auto universe in Q4FY21. Barring 2Ws, PVs and tractors all segments – CVs, 3Ws, and LCVs – have reported sequential volume growth. But the spike in prices of commodities, rubber and crude derivatives will put substantial pressure on margins and earnings for most players. Auto stocks have corrected from the peaks seen last month but continue to be richly valued – much ahead of their long-term P/E multiples. We remain negative on the sector.

**Click here for the full report.**

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## INTERNET TECHNOLOGY

09 April 2021

# Zomato: Leading Indian foodtech play

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**Zomato's latest pre-IPO funding round elevates its valuation to US$ 5.4bn vs. US$ 3.9bn in Dec'20, on the back of (1) recovery from the initial Covid-led volume slump, (2) improving unit economics, and (3) successful listing of US counterpart DoorDash. Despite DoorDash's stronger annual revenue and margins, we believe Zomato's valuation is justified given potential demand scalability in India's growing, duopolistic market. INFOE which holds 18.4% stake (new Zomato-led TP of Rs 2,780 vs. Rs 2,680) remains a SELL because of weakness in its core businesses.**

**KEY RECOMMENDATIONS**

| Ticker | Price | Target | Rating |
|---|---|---|---|
| INFOE IN | 4,842 | 2,780 | SELL |

Price & Target in Rupees | Price as of 8 Apr 2021

**Food delivery business rapidly emerging from Covid slump:** Covid-19 caused food delivery volumes in India to drop 90% during the initial lockdown phase in Mar'20 due to migration away from large cities. For food delivery app Zomato, the pandemic has reduced revenues but accelerated its journey toward profitability as unit economics improved with higher average order value and lower delivery costs, discounts and staff expenses.

**Margins at peak levels; expected to settle lower:** Zomato's margin contribution per order has improved dramatically from a loss of –Rs 47 in Q1FY20 to +Rs 27 in Q1FY21 (Fig 16). Management expects this metric to eventually normalise to Rs 15-20 per order and also indicated that the average monthly burn rate has shrunk from US$ 12mn in FY20 to US$ 1mn in FY21.

**Uptick in GMV:** Zomato's gross merchandise value (GMV) nearly doubled in FY20, partly aided by its Uber Eats acquisition in Jan'20. A swift transition enabled retention of 97% of combined GMV. Following the Covid outbreak, GMV fell 80% from the FY20 peak before returning to 60% of pre-Covid levels in Jul'20.

**Spillover effect from DoorDash valuation:** In Dec'20, US-based food delivery app DoorDash's pre-IPO valuation was pegged at US$ 16bn. Its latest valuation is a whopping US$ 55bn given strong topline growth, high customer retention and a favourable profit trajectory (46% YoY decline in EBITDA loss in FY20).

This stellar valuation appears to have rubbed off on Zomato which closed a US$ 250mn funding round in Feb'21 ahead of its planned IPO later this year (source: media reports), valuing it at US$ 5.4bn from US$ 3.9bn in Dec'20. Although DoorDash operates in a far more mature market, we believe Zomato's valuation is justified given immense growth potential in India's densely populated, digital-driven, duopolistic food delivery market (Swiggy the only credible competition).

## Second wave poses risk to recovery

**Rising Covid-19 infections in India pose a risk to our growth estimate of 11.5% in FY22. As of now, at least seven state governments have imposed some form of restrictions to contain infections. However, consumption led recovery currently underway as seen in higher rural demand and imports, have not been impacted. Tax collections—direct and indirect—have also seen a positive surprise. This along with RBI's GSAP 1.0 program for purchase of Rs 1tn of government securities in Q1 has driven domestic yields lower. But RBI's (5%) and our inflation forecast (4.8%) remains above MPC's target of 4%. This implies India's monetary cycle should see normalisation beginning in H2FY22 with 50bps of repo rate hike in FY23.**

**State specific restrictions to impact growth:** Second wave of infections has hit a number of states led by Maharashtra (13.7% of India's GDP), Karnataka (8%), Gujarat (7.8%), Rajasthan (4.9%), Tamil Nadu (8.5%), Madhya Pradesh (4.2%) and Punjab (2.7%). States have put restrictions to contain the virus. Google mobility index is showing drop in activity across segments, in particular discretionary activities. This, in our view poses downside risk to growth. Our current estimate is 11.5%.

**Tax collections see a positive surprise:** Gross tax collections are likely to see a positive surprise. During Apr-Feb'21, direct tax collections are (-) 10.5% versus FY21RE of (-) 13.8% and indirect tax collections are +7.8% versus FY21RE of +3.6%. This implies fiscal deficit may be 0.5% lower than our estimate of 9.5% of GDP.

**Consumption led recovery:** While rising infections will impact services sector and broader consumption as well, for now high frequency indicators such as PV sales, non-oil-non-gold and electronic imports are resilient. On the agri front, rural demand should remain buoyant with record agri production. This along with impoved rabi sowing and likelihood of normal monsoon bodes well for agriculture growth. At the same time, two-wheeler and CV sales are weaker. Capacity utilisation has now improved to 66.6% (Dec'20) from 63.3% (Sep'20).

**Yields to remain between 6.2-6.5% :** India's 10Y yield fell by 7bps in Mar'21 and further by 9bps in Apr'21. EM yields rose by 28bps. The decrease in Apr'21 is due to RBI's announcement of G-Sec Acquisition Program (GSAP-1) of Rs 1tn in Q1FY22. Centre's H1 borrowing plan is as per expectation at Rs 7.2tn. But is skewed towards long-end (>10 year=69% of issuances). This implies structurally long-end yields are bound to move higher. RBI's inflation forecast till FY23 is above MPC's 4% target. This calls for reduction in corridor between repo and reverse repo in H2FY22, operative rate to be closer to repo rate rather than reverse repo and eventual increase in repo rate in early FY23.

**Depreciation pressure on INR:** INR appreciated by 0.5% in Mar'21 supported by FII inflows (US$ 1.7bn) and lower oil prices. However, INR has depreciated sharply by 2% in Apr'21 amidst a sharp uptick in Covid-19 cases in India. DXY index has strengthened as US economy is likely to show a sharp rebound. In addition to this, current account deficit in India is likely to expand to 1.5% of GDP in FY22 from a surplus of 0.9% of GDP in FY21. Hence, we believe that the pressure on INR will persist


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**AUTOMOBILES** | Q4FY21 Preview | 09 April 2021

# Margins to remain under pressure

**We expect a mixed revenue performance from our auto universe in Q4FY21. Barring 2Ws, PVs and tractors all segments – CVs, 3Ws, and LCVs – have reported sequential volume growth. But the spike in prices of commodities, rubber and crude derivatives will put substantial pressure on margins and earnings for most players. Auto stocks have corrected from the peaks seen last month but continue to be richly valued – much ahead of their long-term P/E multiples. We remain negative on the sector.**

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**OEMs:** Although Maruti (MSIL) has posted a 1% QoQ decline in sales volume, we expect a 3% QoQ increase in Q4 revenue on the back of recent price hikes. However, the sharp upswing in commodity prices makes us skeptical on margins. 2W volumes are down 15% QoQ for Hero (HMCL), 12% for Bajaj Auto (BJAUT) and 7% for TVS Motor (TVSL), while Eicher Motors (EIM – RE) reported 3% QoQ improvement in Q4 dispatches. 2W EBITDA margins and PAT are forecast to decline sharply QoQ due to the rising commodity prices.

In the CV segment, while MHCV sales have improved sequentially alongside improving economic activity, resurgence of the pandemic could delay recovery. We expect Ashok Leyland (AL) to report >40% QoQ revenue growth in Q4 but the spike in metal and tyre costs and its inability to take corresponding price hikes could erode margins going forward.

**Tractors & Tillers:** Tractors growth moderated in Q4. Volumes have fallen 8% QoQ for M&M (MM) while growing 3% for Escorts (ESC). Swaraj Engines (SWE) is expected to post positive growth while volumes for VST tillers were flattish QoQ. Margins for all these agri-related players are projected to decline QoQ given the impact of higher raw material costs, both steel and rubber.

**Tyres:** OEMs have posted sequential growth in MHCV tyre sales. Our channel checks suggest that replacement demand for truck tyres (radials) remains steady. The farm subsegment (tractors) has clocked flattish growth. We expect steady capacity utilisation in bias tyres and project an overall revenue decline of ~2% QoQ for the tyre pack. The sharp jump in rubber prices (from ~Rs 125/kg to Rs 160/kg) and crude derivative costs (+15% QoQ) is expected to shave 350-400bps off Q4 gross margins. We maintain SELL on our entire tyre coverage – CEAT, Apollo Tyres (APTY), MRF, Balkrishna Industries (BIL), TVS Srichakra (TVSS) and JK Tyre (JKI).

## RECOMMENDATION SNAPSHOT

| Ticker | Price | Target | Rating |
|---|---|---|---|
| AL IN | 123 | 60 | SELL |
| BJAUT IN | 3,650 | 2,800 | SELL |
| EIM IN | 2,553 | 2,200 | SELL |
| ESC IN | 1,271 | 1,150 | SELL |
| HMCL IN | 2,928 | 2,900 | SELL |
| MSIL IN | 6,827 | 6,900 | SELL |
| MM IN | 795 | 630 | SELL |
| TVSL IN | 564 | 350 | SELL |
| VSTT IN | 1,843 | 2,300 | BUY |
| APTY IN | 224 | 140 | SELL |
| BIL IN | 1,680 | 1,340 | SELL |
| CEAT IN | 1,540 | 780 | SELL |
| GNA IN | 378 | 450 | BUY |
| JKI IN | 120 | 70 | SELL |
| MDA IN | 102 | 110 | ADD |
| MRF IN | 82,983 | 67,000 | SELL |
| SWE IN | 1,351 | 1,300 | SELL |
| SRTY IN | 1,816 | 1,200 | SELL |

Price & Target in Rupees | Price as of 8 Apr 2021

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**Recommendation scale: 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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